1 FEBRUARY 2023

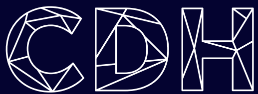
Corporate & Commercial ALERT

IN THIS ISSUE

The rare and elusive fundamental transaction: Statutory mergers and amalgamation in terms of section 113 of the Companies Act

Flexibility and adaptability when advising clients on any proposed transaction, whether a deal with third parties or an internal restructuring, are crucial skills for any mergers and acquisitions (M&A) lawyer. Fortunately, the Companies Act 71 of 2008 (Companies Act) provides a few options, including the rarely used statutory amalgamation or merger in terms of section 113. All distinctions between amalgamations and mergers in drafts of section 113 were removed from the final legislation, so this note only refers to a section 113 merger for convenience.

FOR MORE INSIGHT INTO OUR EXPERTISE AND SERVICES



CLIFFE DEKKER HOFMEYR

INCORPORATING
KIETI LAW LLP, KENYA

The rare and elusive fundamental transaction: Statutory mergers and amalgamation in terms of section 113 of the Companies Act

Flexibility and adaptability when advising clients on any proposed transaction, whether a deal with third parties or an internal restructuring, are crucial skills for any mergers and acquisitions (M&A) lawyer. Fortunately, the Companies Act 71 of 2008 (Companies Act) provides a few options, including the rarely used statutory amalgamation or merger in terms of section 113. All distinctions between amalgamations and mergers in drafts of section 113 were removed from the final legislation, so this note only refers to a section 113 merger for convenience.

Fundamental transactions

Fundamental transactions are dealt with in Part A of Chapter 5 of the Companies Act and are divided into three specific transactions:

1. A disposal or sale of all or the greater part of the assets or undertaking of a company.
2. A scheme of arrangement.
3. A statutory merger.

These are known as "*fundamental transactions*" because they materially alter a company, and once implemented will have a significant effect on the assets and business of a company and the interests of the shareholders of the company. The Companies Act sets out very specific requirements for each of the fundamental transactions, and aligned South African law with international best practices. The section 113 merger provisions, read with section 116 of the Companies Act, in particular, seem to mirror the requirements and procedures adopted in most other progressive jurisdictions, including the US. This article looks at the use of section 113 mergers and the impact of a recent change to how the registration or endorsement confirming transfer of immovable property pursuant to a section 113 merger is dealt with by the Deeds Office, and the subsequent cost implications.

Disposals and schemes of arrangement are commonplace in the M&A space. Section 113 mergers are far rarer in practice and seem to be an under-appreciated tool, although this may be because there is a dearth of case law dealing with them.

Section 113 contains a mechanism for two or more profit companies (state-owned, public, private and personal liability companies) to merge, and allows for all assets and liabilities of the companies involved (merging companies) to be reorganised and transferred into the

The rare and elusive fundamental transaction: Statutory mergers and amalgamation in terms of section 113 of the Companies Act

CONTINUED

merged or surviving company/ies, by operation of law. Two typical structures of a section 113 merger are:

1. Existing company A (merging company) merges into existing company B and company B (merged company) survives and company A's existence terminates.
2. Existing companies A and B merge into a new merged company C and both companies A and B's existence terminates.

Ultimately, a merger results in the dissolution of one or more of the entities involved and may involve the creation of an entirely new company.

Advantages of a statutory merger

In a typical sale of business, parties are required to assign individual contracts, including loan agreements, supply contracts, leases, and sometimes hundreds or thousands or of contracts with customers. Opting for the statutory merger has several advantages, but undoubtedly, the most valuable is the transfer of all of the 'disappearing' company's assets and liabilities to the merging or surviving company, by operation of law. Practically, this means that, unless the contract prohibits the transfer by section 113 merger or includes the specific right to terminate the contract upon the occurrence of a merger, all contracts of the affected companies are automatically transferred by operation of law, without the consent of counterparties to contracts. This, despite an express requirement in the contract to obtain consent in the event of an assignment because the transfer would take place by operation of law, and not by assignment,

Section 113 therefore enables companies to drastically reduce the costs and legal formalities normally required for the transfer of a business from one company to another. Similarly, generally licences and permits are also transferred by operation of law, without a requirement to apply for them to be transferred, subject to the surviving entity continuing to meet any relevant conditions. Notably, the statutory merger is the only fundamental transaction mechanism that occurs by operation of law, while in a scheme of arrangement and a section 112 disposal, the parties are required to comply with the relevant legal formalities for the transfer of assets and liabilities. Hence, a statutory merger is ideal in scenarios involving businesses with multiple standard form contracts, where obtaining third-party consent to an assignment is impractical.

Immovable property exception

Although all of the assets and liabilities of the merging or surviving companies are transferred by operation of law, without the need for any additional formalities, there is an exception in relation to immovable property, contained in section 116(8) of the Companies Act, which requires that in order for any property that is registered in terms of any public regulation (including immovable property) to be transferred from a

The rare and elusive fundamental transaction: Statutory mergers and amalgamation in terms of section 113 of the Companies Act

CONTINUED

merging company to the merged company, a copy of the merger agreement, together with a copy of the filed notice of merger must be lodged with the keeper of the relevant property registry (i.e. the Deeds Office in the case of immovable property) to effect a transfer of the registration of that property. To date, it was possible to effect a transfer of the registration of immovable property without adhering to all of the formalities prescribed by the Deeds Registries Act 47 of 1937. This was achieved through a section 3(1)(v) application and registration could simply be effected by attaching a copy of the merger agreement together with a filed notice of merger. An endorsement would then be made on the relevant title deeds of the properties of the 'disappearing' company.

However, as per the Chief Registrar's Circular No 1 of 2022, issued on 16 May 2022, the section 3(1)(v) application must now include a transfer duty receipt/exception certificate and a rates clearance certificate. This has the effect of dramatically increasing the costs associated with this M&A procedure in instances where there are immovable properties (and accompanying bonds) which need to be transferred, as the conveyancing work involved is akin to a regular transfer of immovable property.

Requirements for a statutory merger

Section 113 is prescriptive regarding the information required in the merger agreement, but allows for a degree of flexibility, particularly regarding the consideration that may be paid. It references the traditional merger transaction, where shares in the merging companies are converted into shares into the merged entity whilst allowing other forms of consideration, including settling the shareholders of one or more of the merging entities in cash.

Importantly, the section requires that the board of each amalgamating or merging company confirm their reasonable belief that such company will satisfy the solvency and liquidity test set out in section 4 of the Companies Act, before submitting the merger agreement to shareholders for approval. A notice must also be sent to the creditors notifying them of their right to apply to a court for a review of the merger on the grounds that the creditor will be materially prejudiced by the merger. Finally, from a regulatory perspective, a section 113 merger may also constitute an affected transaction if it involves a regulated company, requiring approval by the Takeover Regulation Panel and may also require Competition Commission approval.

Conclusion

Ultimately, the chosen mechanism for a specific transaction is dependent on several factors, including the practical, regulatory, cost and tax implications associated with it and a statutory merger certainly is a useful tool in the right circumstances.

Shameegh Allen, David Thompson and Robin Henney

OUR TEAM

For more information about our Corporate & Commercial practice and services in South Africa and Kenya, please contact:

Willem Jacobs
Practice Head & Director:
Corporate & Commercial
T +27 (0)11 562 1555
M +27 (0)83 326 8971
E willem.jacobs@cdhlegal.com

David Thompson
Deputy Practice Head & Director:
Corporate & Commercial
T +27 (0)21 481 6335
M +27 (0)82 882 5655
E david.thompson@cdhlegal.com

Sammy Ndolo
Managing Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E sammy.ndolo@cdhlegal.com

Roelof Bonnet
Director:
Corporate & Commercial
T +27 (0)11 562 1226
M +27 (0)83 325 2185
E roelof.bonnet@cdhlegal.com

Tessa Brewis
Director:
Corporate & Commercial
T +27 (0)21 481 6324
M +27 (0)83 717 9360
E tessa.brewis@cdhlegal.com

Etta Chang
Director:
Corporate & Commercial
T +27 (0)11 562 1432
M +27 (0)72 879 1281
E etta.chang@cdhlegal.com

Vivien Chaplin
Director:
Corporate & Commercial
T +27 (0)11 562 1556
M +27 (0)82 411 1305
E vivien.chaplin@cdhlegal.com

Clem Daniel
Director:
Corporate & Commercial
T +27 (0)11 562 1073
M +27 (0)82 418 5924
E clem.daniel@cdhlegal.com

Dane Kruger
Director:
Corporate & Commercial
T +27 (0)21 481 6362
M +27 (0)74 914 1402
E dane.kruger@cdhlegal.com

Jenni Darling
Director:
Corporate & Commercial
T +27 (0)11 562 1878
M +27 (0)82 826 9055
E jenni.darling@cdhlegal.com

André de Lange
Sector Head: Agriculture, Aquaculture
& Fishing Sector
Director: Corporate & Commercial
T +27 (0)21 405 6165
M +27 (0)82 781 5858
E andre.delange@cdhlegal.com

Andrew Giliam
Director:
Corporate & Commercial
T +27 (0)21 481 6363
M +27 (0)83 359 7069
E andrew.giliam@cdhlegal.com

John Gillmer
Joint Sector Head: Private Equity
Director: Corporate & Commercial
T +27 (0)21 405 6004
M +27 (0)82 330 4902
E john.gillmer@cdhlegal.com

Allan Hannie
Director:
Corporate & Commercial
T +27 (0)21 405 6010
E allan.hannie@cdhlegal.com

Ian Hayes
Director:
Corporate & Commercial
T +27 (0)11 562 1593
M +27 (0)83 326 4826
E ian.hayes@cdhlegal.com

Peter Hesseling
Director:
Corporate & Commercial
T +27 (0)21 405 6009
M +27 (0)82 883 3131
E peter.hesseling@cdhlegal.com

Quintin Honey
Director:
Corporate & Commercial
T +27 (0)11 562 1166
M +27 (0)83 652 0151
E quintin.honey@cdhlegal.com

Brian Jennings
Director:
Corporate & Commercial
T +27 (0)11 562 1866
M +27 (0)82 787 9497
E brian.jennings@cdhlegal.com

Rachel Kelly
Director:
Corporate & Commercial
T +27 (0)11 562 1165
M +27 (0)82 788 0367
E rachel.kelly@cdhlegal.com

Yaniv Kleitman
Director:
Corporate & Commercial
T +27 (0)11 562 1219
M +27 (0)72 279 1260
E yaniv.kleitman@cdhlegal.com

Justine Krige
Director:
Corporate & Commercial
T +27 (0)21 481 6379
M +27 (0)82 479 8552
E justine.krige@cdhlegal.com

Jaco Meyer
Director:
Corporate & Commercial
T +27 (0)11 562 1749
M +27 (0)83 477 8352
E jaco.meyer@cdhlegal.com

OUR TEAM

For more information about our Corporate & Commercial practice and services in South Africa and Kenya, please contact:

William Midgley
Sector Head: Commercial Real Estate
Director: Corporate & Commercial
T +27 (0)11 562 1390
M +27 (0)82 904 1772
E william.midgley@cdhlegal.com

Tessmerica Moodley
Director:
Corporate & Commercial
T +27 (0)21 481 6397
M +27 (0)73 401 2488
E tessmerica.moodley@cdhlegal.com

Anita Moolman
Director:
Corporate & Commercial
T +27 (0)11 562 1376
M +27 (0)72 252 1079
E anita.moolman@cdhlegal.com

Wayne Murray
Director:
Corporate & Commercial
T +27 (0)21 405 6018
M +27 (0)79 691 0137
E wayne.murray@cdhlegal.com

Francis Newham
Executive Consultant:
Corporate & Commercial
T +27 (0)21 481 6326
M +27 (0)82 458 7728
E francis.newham@cdhlegal.com

David Pinnock
Joint Sector Head: Private Equity
Director: Corporate & Commercial
T +27 (0)11 562 1400
M +27 (0)83 675 2110
E david.pinnock@cdhlegal.com

Allan Reid
Joint Sector Head: Mining & Minerals
Director: Corporate & Commercial
T +27 (0)11 562 1222
M +27 (0)82 854 9687
E allan.reid@cdhlegal.com

Jess Reid
Director:
Corporate & Commercial
T +27 (0)11 562 1128
M +27 (0)83 571 6987
E jess.reid@cdhlegal.com

Megan Rodgers
Sector Head: Oil & Gas
Director: Corporate & Commercial
T +27 (0)21 481 6429
M +27 (0)79 877 8870
E megan.rodgers@cdhlegal.com

Ludwig Smith
Director:
Corporate & Commercial
T +27 (0)11 562 1500
M +27 (0)79 877 2891
E ludwig.smith@cdhlegal.com

Tamarin Tosen
Director:
Corporate & Commercial
T +27 (0)11 562 1310
M +27 (0)72 026 3806
E tamarin.tosen@cdhlegal.com

Roxanna Valayathum
Director:
Corporate & Commercial
T +27 (0)11 562 1122
M +27 (0)72 464 0515
E roxanna.valayathum@cdhlegal.com

Roux van der Merwe
Director:
Corporate & Commercial
T +27 (0)11 562 1199
M +27 (0)82 559 6406
E roux.vandermerwe@cdhlegal.com

Andrew van Niekerk
Head: Projects & Infrastructure
Director: Corporate & Commercial
T +27 (0)21 481 6491
M +27 (0)76 371 3462
E andrew.vanniekerk@cdhlegal.com

Charl Williams
Director:
Corporate & Commercial
T +27 (0)21 405 6037
M +27 (0)82 829 4175
E charl.williams@cdhlegal.com

Njeri Wagacha
Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E njeri.wagacha@cdhlegal.com

Christelle Wood
Director:
Corporate & Commercial
T +27 (0)11 562 1372
M +27 (0)83 498 2850
E christelle.wood@cdhlegal.com

Emma Hewitt
Practice Development Director:
Corporate & Commercial
T +27 (0)11 562 1635
E emma.hewitt@cdhlegal.com

BBBEE STATUS: LEVEL ONE CONTRIBUTOR
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.

PLEASE NOTE
This information is published for general information purposes and is not intended to constitute legal advice. Specialist legal advice should always be sought in relation to any particular situation. Cliffe Dekker Hofmeyr will accept no responsibility for any actions taken or not taken on the basis of this publication.

JOHANNESBURG
1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa.
Dx 154 Randburg and Dx 42 Johannesburg.
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E jhb@cdhlegal.com

CAPE TOWN
11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E ctn@cdhlegal.com

NAIROBI
Merchant Square, 3rd floor, Block D, Riverside Drive, Nairobi, Kenya. P.O. Box 22602-00505, Nairobi, Kenya.
T +254 731 086 649 | +254 204 409 918 | +254 710 560 114
E cdhkenya@cdhlegal.com

STELLENBOSCH
14 Louw Street, Stellenbosch Central, Stellenbosch, 7600.
T +27 (0)21 481 6400 E cdhstellenbosch@cdhlegal.com

©2023 11890/FEB

CDH
CLIFFE DEKKER HOFMEYR

INCORPORATING
KIETI LAW LLP, KENYA