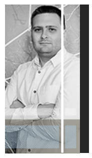

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The big five amendments proposed by the Companies Amendment Bill, 2018

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The Companies Amendment Bill, 2018 (the "**Bill**") was released for public comment by the Minister of Trade and Industry on 21 September 2018. The Bill, if introduced in its current form, proposes a number of changes to the Companies Act, 2008. This snapshot review deals with only our "big five" amendments.

1. Limiting the scope of financial assistance under section 45

The Bill proposes to limit the net of financial assistance transactions that fall within section 45 by excluding "the giving by a company of financial assistance to, or for the benefit of, its own subsidiary." The intention behind this exclusion is laudable, but its implementation is questionable. Our issues are as follows:

- The exclusion uses the specific language of "its own subsidiary". Section 3 of the Companies Act defines what is regarded as a subsidiary very broadly; namely a company is a subsidiary of another juristic person if that juristic person or "one or more other subsidiaries of that juristic person" directly or indirectly control the company. Does the reference to "its own subsidiary" limit this exclusion to only subsidiaries of the juristic person which are held directly by the juristic person? This is not clear.
- Why has the limitation been broadened to all subsidiaries whereas, it is submitted, it should only apply to wholly owned subsidiaries that are excluded under section 45? This is because it is difficult to see any mischief arising in a wholly owned relationship but there is potential mischief in a relationship that involves outside minority shareholders.
- The exclusion is, respectfully submitted, in the wrong place. It purports to exclude financial assistance to subsidiaries from the operative provision of section 45(2) – but section 45(2) merely empowers the board to give financial assistance "subject to subsections (3) and (4)". Does this mean that financial assistance to a company's own subsidiary is therefore not within the remit of the board's authority, regardless of whether it can comply with subsections (3) and (4)? This is not in line with the overview of the Bill on this amendment contained in paragraph 3.11 which states that the purpose is to exclude financial assistance by a company to its subsidiary. This exclusion should therefore be structured as an exclusion to the requirements in subsections (3) and (4).
- The aforementioned overview of the Bill states that the provision of financial assistance by a company to its subsidiaries "does not need the adoption of a special resolution". This commentary is problematic as, it is well known, a special resolution is but one of the many requirements applying financial assistance that falls within section 45. The commentary therefore differs materially from the ambit of the language of the exclusion such that there may be a conservative interpretation that interprets the exclusion as only excluding the requirement for a special resolution.
- In many cash sweep management programmes, the cash sitting in the account of subsidiaries that operate and generate profit, are swept into a broader account that minimises the interest costs of other subsidiaries. These sweeps, resulting in intra-group loan liabilities, between commonly held subsidiaries and between such subsidiaries and the holding company will continue to be plagued by compliance with section 45. This is because the exclusion only applies downwards, and not horizontally or upwards, leading to a continued cost of compliance with section 45. In addition, wholly owned foreign corporations under the control of a company remain within the reach of section 45 requiring compliance even though, in substance, there may be no material difference between a foreign subsidiary and a local one.

2. Private companies as regulated companies

Section 118(1)(*c*)(i) of the Companies Act mainly regards private companies as regulated companies if more than 10% of its issued securities had been transferred, other than between related or inter-related persons, within a 24-month period prior to the date of the affected transaction. This regime is sought to be replaced with a regime that only regards private companies as regulated companies if the private company is required by the Companies Act or the regulations to have its annual financial statements audited every year. Our commentary appears below:

- Existing transactions that are in place at the time of the Bill being validly passed and promulgated, will presumably continue to apply under old regime. This is because the minority shareholders may, depending on the timing, have a right that has accrued in law to them. This depends, it is submitted, on an interpretation as to when "the time of the relevant affected transaction" occurs.
- Section 118(2) has not been proposed to be deleted, which empowers the Minister to prescribe the relevant percentage of issued securities that would, if transferred within the 24-month period, cause the private company to be a regulated company. Regulation 91 operates on the basis of this empowering provision. Our suggestion to the Department of Trade and Industry is that this error be rectified by the inclusion of the proposed deletion of section 118(2) as well, so that the new regime replaces wholesale the former.

3. When does the amendment to a memorandum of incorporation take place?

One of the proposed amendments seeks to clarify this question on which practitioners appear to have been divided based on the definition of "file". Without resolving the debate in favour of any side, it will be clear that going forward, the CIPC has 10 days after receipt of the notice of amendment to reject the notice of amendment. Notice of rejection is not enough – it needs to be supplemented with reasons. So, if the CIPC is inactive and has not responded within 10 business days, it appears to be estopped from forever doing so notwithstanding that it may have good cause to do so. A word of caution on drafting condition precedents that require the memorandum of incorporation to be amended (without a name change) that provision should still be made for the deemed delivery time periods in table CR3 to be taken into account.

4. The danger of the new section 38A

One of the proposed new amendments is to include the power of the court, upon application by an interested person or by the company, to order that shares that were created, allotted or issued invalidly or in an unauthorised manner, to be validly created, allotted or issued if it is "just and equitable" to do so. No reference is made to the plight of the existing shareholders and their say of whether they would prefer the admittance of a new shareholder.

What is "just and equitable" will, no doubt, depend on the facts of each particular case but it cannot be just to enable an outside person to be permitted to be a shareholder, notwithstanding the harm to such person, if the existing body of shareholders have not approved such "retroactive authorisation" in terms of section 38(2). Section 38(3)(*a*) is clear that a share issue is a nullity if it exceeds any authorisation and a shareholder resolution under section 38(2) has not been passed. The new section 38(A) does not appear to be constrained by this fact and may operate as another bite at the cherry for the purported shareholder.

In addition, no provision is made for the period between the application and any resultant court order. For instance, how are resolutions meant to be passed during this period – does the purported shareholder have a right to be present and to vote? This issue does not arise in section 38(2) because there is a limited duration for a retroactive resolution to be passed (60 business days) but this period can be substantially longer with a court application. The issue arises as the proposed section 38A(3) states that "the shares must be deemed to have been validly created… upon the terms of the creation." One of the terms of creation is the date of creation, and therefore this will be a problematic provision going forward unless a court could be swayed to impose a condition that stipulates that the date of creation is a later date.

It is also clear that provision should be made in a company's memorandum of incorporation for as much of the governance regime as possible as, if another shareholder is admitted, it would *ipso facto* bind them – as opposed to including provisions in a shareholders agreement which would not.

5. A new type of post-commencement financing ("PCF")

Section 135(1A) proposes to deem, as PCF, an amount equal to all disbursements, outgoings, including rates, taxes, electricity and water, paid by a property owner to a third party. These claims will rank equally to claims for outstanding remuneration during business rescue proceedings to employees in terms of section 135(1) of the Companies Act, but higher than PCF. It remains open if (i) a landlord would be able to recoup the amount of income tax owing to The South African Revenue Service in relation to the rental that would have accrued during such period; (ii) a rental subcontract would be included within this construct.

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