THE BANKING ASSOCIATION SOUTH AFRICA

Tel +27 11 645 6700
Fax +27 11 645 6800
P O Box 61674
Marshalltown 2107
www.banking.org.za

3rd Floor Building D
Sunnyside Office Park
32 Princess of Wales Terrace
Parktown 2193

30 July 2008

The Chair
Portfolio Committee on Trade and Industry
Parliament

Doc Ref: STUARTG/MARKET CONDUCT/#42394_V1

Your ref:

Direct ☎: (011) 645-6714

E-⌧: stuartg@banking.org.za

Attention: Ms M A Williams
mawilliams@parliament.gov.za

Dear Sir

COMMENTS: DRAFT COMPANIES BILL (B61-2008)

With reference to the above-mentioned Bill, and the scheduled Portfolio Committee public meetings on it (11 – 15 August 2008) we welcome the opportunity to provide comments on the draft Bill, but must first express our concern at the short time that has been provided to the public to study the Bill, develop appropriate comments, mandate these comments as required and then submit them for consideration. This short lead time is particularly serious as the Bill is a total rewrite of the companies' regulatory framework, and care needs to be taken to prevent any unintended consequences.

We therefore make the following comments on the Bill and its Explanatory Memorandum, subject to concerns about the lack of time for proper in-depth analysis and consultation on the detailed Bill. We would also request an opportunity to address some of these issues personally with the Committee during its public hearings, if possible on Wednesday 13 August 2008 (due to prior staff commitments).

1. Comments – Memorandum on the Objects of the Companies Bill, 2008.

1.1 Section 2 – Overall plan for company legislation.

The second paragraph refers to the "co-existence of the new Companies Act, 1973 and the Close Corporations Act, 1984..." This reference should presumable be "2008" (or as applicable) and not 1973.

The new Companies Bill once enacted will close the Close Corporations Act, 1984 for the formation of new Close Corporations. The intention is that, from that time on, small companies should incorporate themselves under the new Companies Bill, 2008. While this objective is desirable, there may be a challenge for the persons wishing to establish a small company (or Close Corporation equivalent), as they would have to be totally knowledgeable of the new Companies Bill, 2008 (about 214 pages) vs. ± 35 pages for the Close Corporations Act, 1984.

It is recommended that some consideration be given to publishing a "small companies schedule" that would entail just those sections of the new Bill that

Registration Number: 1992/001350/08 An Association incorporated under Section 21 of the Companies Act 1973
Directors: S Booysen (Chairman), C Coovadia (Managing), TA Boardman, S Koseff, C Low*, J Maree, S Nxasana, Ms D Oosthuyse**, R Stassen, D Woollam **Company Secretary:** JM Hulley (*British) (**American)

relate to such small companies (e.g. as in the schedule for non-profit companies).

1.2 **New body – Companies Ombud.**

The Bill creates a new "alternative dispute resolution" mechanism via a statutory "Companies Ombud". However, the roles and duties of this new Ombud as specified in various sections of the Bill would appear to be confused, and it is recommended that specific consideration be given to this aspect.

An "Ombud" is per definition a "no-charge" alternative dispute resolution mechanism between institutions and <u>consumers</u>. It provides a quicker (and obviously free) mechanism for consumers to have their complaints investigated, mediated or adjudicated. It is not anticipated, however, that there will be many consumer-related complaints under this Bill, as the Bill does not deal with normal supply of products or services.

On the other hand, most of the roles and duties assigned to the "Companies Ombud" in the Bill relate more to an appeal tribunal than an Ombud, as they relate to companies or incorporators complaining about administrative actions by one or other of the regulatory bodies under the new Bill. It is recommended that the description of the "Companies Ombud" be changed throughout the Bill to "Companies Tribunal," or some equivalent administrative and appeal body. This will still ensure that the objective envisaged by the Bill is achieved, without any confusion in the market relating to the concept "Ombud".

1.3 **Business rescue provisions – the "supervisor"**

The entire new business rescue process relies on the creation of a new statutory-regulated profession of business turnaround strategists called "supervisors". These skilled professionals are not currently available in the economy in anything like the potential numbers that will be required for the whole business rescue intervention. The existing body of professional liquidators and judicial managers is not necessarily skilled in this context, given their historic focus on liquidations and insolvencies (i.e. realising asset value, not improving company performance). Experience with the implementation of the National Credit Act supports the position that the full implementation of the new business rescue regime should be delayed until such time as there are sufficient "supervisors" registered and capable of coping with all the new business rescue applications, failing which creditors should be entitled to exercise their full rights.

1.4 **Business rescue provisions – power of the supervisor to cancel or amend any contracts**

The Bill enables the supervisor to unilaterally cancel or amend any condition of any agreement. While the capability of the supervisor to renegotiate certain contractual terms is understood, this particular breach into the sanctity of the law of contract is a particular concern, as it would impact every single contract at the time such contract is being negotiated, with increased risk and consequential price. In the specific instance of banks as creditors, it could mean that all security offered for loans is suspect (i.e. can be unilaterally overturned by a supervisor), and this would have severe banking supervisory and regulatory costs (i.e. increased provisions for bad debts, as the security provided could not be relied upon contractually). We strongly recommend that the supervisor's powers to effect any such contractual amendments be reviewed.

1.5 **Disclosure requirements**

Schedule 4 of the existing Companies Act, 1973 has not been included in its entirety in the Bill. We support this. Most of the requirements in Schedule 4 are disclosure-based and as the Bill requires financial statements to be prepared in accordance with IFRS, the need for duplicate disclosure requirements is done away with. However, not all of the requirements listed in Schedule 4 are required by IFRS. We are of the opinion that several of the requirements that are not required in terms of IFRS, could enhance financial statements and should be included in the Bill. In this context we therefore recommend that the following disclosures should be mandatory in terms of the Bill:

- The amount of share capital or number of shares which directors are authorized to issue as well as the terms of such authority and the period for which the authority was granted;
- Instances where assets have been pledged as security for third parties' liabilities;
- Disclosure of the nature of and the exchange rates actually used in the preparation of financial statements;
- Fees paid to auditors.

1.6 **Rights of shareholders**

Shareholders have limited rights during rescue proceedings (Chapter 6 of the Bill), for instance, they cannot resolve that the company be placed in business rescue. They can however bring a court application. They have no right to vote on the approval of the rescue plan unless their rights are negatively affected.

Preference shareholders and ordinary shareholders are treated equally. This could have a negative impact on preference share funding in general and on the pricing of preference share funding specifically.

Secured creditors and concurrent creditors are treated equally - the only issue that matters is the value of the outstanding debt. We believe secured creditors should have stronger protection, e.g. they should have the right to continue legal proceedings or exercise security after a finite period (of not more than 30 business days) from when the business rescue proceedings commenced. This could mitigate the negative effects on risk mitigation in terms of Basel II (see discussion of impact on Basel II below).

2. **Comments – Bill**

2.1 **Section 1 – Definitions**

Ad definition of "*agreement*": Agreement is defined to include an arrangement that <u>purports</u> to create rights and obligations. Purport is defined in the Oxford Dictionary, Tenth Edition, as "appear to be or do, especially falsely". An agreement is either an agreement, as defined in law, or it is not. Therefore an agreement will create rights and obligations and it will not purport to create rights and obligations (see for example the use of the word "agreement" in Subsection37(7)(a) - if interpreted literally it can refer to a purported arrangement or understanding instead of an actual agreement). It is recommended that the words "purports to" be deleted from this definition.

Ad definition of "*director*": The definition of "director" is very narrow. The existing Companies Act, 1973 defines a "director" as "*a director appointed as such and any other person occupying the position of director or alternate*

director by whatever name he may be designated". The definition in the Bill, namely a person being a member of the board of a company, could see a person escaping liability as a director if he or she is not formally appointed as a member of the board, but factually occupies the position of a director. Consideration should be given to retaining the existing definition.

Ad definition of "*distribution*": In paragraph (b) of the definition, the impact of the words "*for the benefit of*" may create uncertainty. If, for example, a company incurs a loan in order to on-lend the debt to one of its subsidiaries, should this actually constitute a "distribution"? If it is waived or forgiven as stipulated in (c) it is appropriate (i.e. a distribution) but not simply if it is incurred. It is recommended that this subsection be clarified to make its intention clearer. Note: substitute "is" with "in" in subsection (a)(iii).

Ad definition of "*financial statement*": Taking into account the use of the words annual financial statements, read with the definition of "financial statement", it should be considered whether a more restrictive definition of annual financial statements may not be required. For example, should the words "financial statements" be attributed the meaning given in the proposed definition, the phrase annual financial statements would be too widely interpreted while they should mean something very specific. In Subsection 26(1)(a)(i) it is stipulated that a shareholder shall have the right to inspect the "annual financial statements" mentioned in Subsection 24(3)(c)(ii). According to the proposed definition of financial statement this would include all interim or preliminary reports, whereas these not be freely available to shareholders.

Ad definition of "*knowing, knowingly or knows*": We recommend that the word "could" in both paragraphs (b)(ii) and (iii) should be replaced with the word "would". To illustrate our concern about the word "could": if a proper investigation "could" have provided a person with actual knowledge, but it did not, the person could still be deemed to have known. This is unreasonable and can imply strict liability.

Similarly, we believe that although someone may objectively (according to a test involving reasonability) be deemed to have known if such person did not take reasonable measures or made reasonable investigations, he/she should still be able to prove that he/she did not know even despite these measures or investigations. Accordingly we propose the following new subsections for paragraph (b):

"(ii) investigated the matter to a reasonable extent, and such investigation would have provided the person with actual knowledge, unless the person proves it did not; or

(ii) taken other reasonable measures which, if taken, would be expected to have provided the person with actual knowledge of the matter, unless the person proves it did not;"

Ad definition of "*special resolution*": there is no provision anywhere in the Bill for special resolutions to be registered with the appropriate regulatory authority. The current Act contains this requirement, and we recommend that the Bill provide that the special resolutions should be filed given the wide impact that such special resolutions can have.

Both the terms "*share*" and "*securities*" are defined in the Bill. The term "*securities*" bears the meaning assigned to it in the Securities Services Act, 2004 and is a much wider meaning than "*share*" (see below for more detail). However, the terms appear to be used indiscriminately and interchangeably in

the Bill. The consequences of such indiscriminate use are significant, and we recommend that the drafters scrutinise the use of these terms carefully to ensure that the correct meaning is encapsulated in the various sections.

[Note: The definition of "securities" in the Securities Services Act, 36 of 2004, reads –

"securities" –

(a) means –

(i) shares, stocks and depository receipts in public companies and other equivalent equities, other than shares in a share block company as defined in the Share Blocks Control Act, 1980 (Act No. 59 of 1980);.."

No reference is made in the definition to shares held in private companies and this is an anomaly. The context to which "securities" is used in the Bill indicates that the term "securities" should also include companies which are private companies. Changes are required to bring the definition in line with the intention of the Bill and to include private companies. However, although this is appropriate for Chapter 6 of the Bill, it is not appropriate in all other instances.]

2.2 Section 2 – Related and inter-related persons, and control

Section 2 of the Bill would appear not to include a situation where a company or a juristic person (as defined) may be related to and/or controlled by a close corporation. We recommend that the Bill be amended to include a provision to cater for this.

The Bill protects, amongst others, shareholders by ensuring that corruption and collusion between companies, directors and shareholders is minimised. Subsection 2(1)(d) of the Bill, however, casts the net very wide. As a result persons far removed from one another may be considered related parties. It is recommended that a more restrictive definition be included, bearing in mind the provisions of subsection 2(3), to avoid undue burden. For example, subsection 75(6) compels a director to disclose the fact that a person "related" to him/her has acquired a financial interest in the company of which he/she is a director. From the wording of the definition in subsection 2(1)(d) it is conceivable that the director in question may not even be aware that the "related" person has acquired the financial interest. Consider restricting the definition of "inter-related persons" by inserting a provision that will exempt a person from the provision of the Act in respect of matters arising because of the relationships contemplated in subsection 2(1), if the person could not be reasonably expected to have had knowledge of such relationship.

2.3 Section 3 – Subsidiary relationships

The definition of "*wholly-owned subsidiary*" in subsection 3(1)(b) is significantly different from that in the International Financial Reporting Standards (IFRS), with which companies must comply (subsection 29(5)(b)). We recommend that the definition in subsection 3(1)(b) be amended to refer to the IFRS to eliminate interpretation difficulties.

2.4 Section 4 – Solvency and liquidity test

Section 4 sets out the liquidity and solvency requirements, which are required to be met at a "*particular time*". Does "particular time" imply that directors

must continuously monitor that the solvency and liquidity requirements of the Bill are being met? In this regard also see the comments on section 22 below.

Subsection 4(1)(a) states that the solvency and liquidity tests are satisfied if "*the assets of a company, or, if the company is a member of a group of companies, the consolidated assets of the company, as fairly valued, equal or exceed the liabilities of a company or, if the company is a member of a group of companies, the consolidated liabilities of the company, as fairly valued*".

The interpretation of this section in the context of groups needs to be considered, for example:

> Company A owns 100% of B and C. B's assets exceed its liabilities whilst C's assets are less than its liabilities. Group A's assets exceed its liabilities on a consolidated basis. Does Section 4 imply that Company B is able to make a distribution without violating s4, despite Company C's liabilities exceeding its assets?

The following additional questions require consideration:

- Is it the intention of the Bill that the term 'assets' only refers to recognised assets of a company or group of companies? Since subsection 4(2)(b)(i) includes contingent assets (and liabilities) it could be argued that the term 'assets' extends to unrecognized assets (in accounting terms);
- Is it the intention of the Bill to include 'intangible assets' such as customer lists, brands and trademarks? If 'assets' does indeed extend to such 'intangible assets' this subsection becomes increasingly impractical and costly to implement, as the valuation of intangibles is difficult, costly and takes considerable time and effort. Furthermore, any such valuation would have a number of subjective references.

The subsection also refers to "*a member of a group of companies*". A <u>member</u> is only defined by the Bill in relation to a non-profit company. What is the definition of a member in terms of this subsection? If this refers to any company, then any associate or joint venture could be seen as a member of a group despite the group not being able to control the associate or joint venture in any way. It is recommended that <u>member</u> be clearly defined to prevent any interpretation difficulties.

It should be noted that in practice it would be extremely difficult for any director of a company which is exempted from producing financial statements to properly apply the solvency and liquidity tests (per subsection 4(2)) in the dealings of the company. It may be prudent for the Bill to be amended to ensure that in the case of such companies (i.e. those that do not have to prepare proper financial statements) the directors of such companies are treated differently from directors of companies which have those obligations.

Subsection 29(5)(b) requires companies to comply with the International Financial Reporting Standards. There are explicit standards under IFRS relating to the determination of "fair value", as required under section (4). However, there are no provisions in this standard for "any other valuation…" as per subsection 4(2)(b)(ii). It is recommended that this subsection be deleted in order to ensure internal consistency within the Bill.

2.5 Section 5 – General interpretation of Act

We suggest that the reference in Subsection 5(3)(c) should be to any "public holiday **<u>in the Republic of South Africa</u>**".

The section states that, should there be an inconsistency between another Act and the Bill, and the other Act and the Bill cannot be applied concurrently, the Bill shall prevail (except in instances where other Acts, which are listed, prevail). The Bill will therefore take precedence over the Banks Act, should the Banks Act and the Bill be in conflict, unless it is clear that the Banks Act prevails (see in this regard section 51(1) of the Banks Act). The predominance of the generic Bill over the specialist Banks Act could result unintended consequences in the financial sector. It is therefore recommended that the Banks Act, 1990 be included in the list of Acts in subsection 5(4)(b)(i).

2.6 Section 6 – Anti-avoidance, exemptions and substantial compliance

The purpose of having records, such as annual reports, submitted electronically is to avoid the costs of printing (which may not be considered "reasonable"). Concepts such as "reasonable time" and "reasonable cost" are subjective and could lead to unnecessary disputes. It is recommended that the reference to "within a reasonable time and at a reasonable cost" in subsections 6(10) and (11) be deleted.

The Bill does not specify whether an "electronic signature" or "advanced electronic signature", as defined in the ECT Act, is required in subsection 6(12)(a). The Bill should state whether "electronic signature" or "advanced electronic signature", as defined in the ECT Act, is required. Similarly, subsection 6(12)(b) should be amended to provide for electronic signatures, as specified above.

2.7 Section 11 – Criteria for names of companies

Many companies in national or multi-national groups use similar brands or names. They may even have a similar registered name to other companies in the group. Further, many groups register their trademarks in the name of one specific entity within that group for purposes of effective administration and enforcement. Subsection 11(2) would seem to apply "across the board", and we recommend that it be amended to make provision for the use of similar names and trademarks within groups of companies. Such an exemption will not compromise the general protections required under the Bill.

2.8 Section 12 – Reservation of name for later use; Section 14 – Registration of a company

These sections include both the SA Human Rights Commission and the new Companies Ombud in issues of name reservation. It is unclear why the Human Rights Commission should in any way be involved, and an "Appeals Tribunal" may be more appropriate than an Ombud.

Section 12 would appear to prohibit the "defensive" registration of company names, in order to prevent them being abused by "lookalikes". It remains to be seen whether the new registration criteria in section 11 are implemented strongly enough to continue to provide companies with adequate protection in this regard, e.g. a person may reserve a name and a translation of that name into the 11 languages as well as abbreviations. Upon registration only one name will however be registered, as there is no provision for the translated names to be registered as well. How would this be dealt with if another person tried to register a similar or same name in one of the other languages?

2.9 Section14 – Registration of company

Confusion may be introduced into the market in that a company may be incorporated (in terms of section 13) before it has established whether or not

the requested name is available. In the case of an unsuitable name section 14 provides for the company to be registered using the company's registration number followed by 'Inc.', '(Pty) Ltd' or whichever applicable, as an interim name. The question then arises whether the company is able to contract under the interim name (and the answer is presumably "yes"), and if so, where a company is granted an interim name as a result of the requested name being the same as another company (as per subsection 14(2)(b)), how would possible infringement by the interim name of the trademark or trade name of such other existing company be dealt with? We suggest that the Bill be amended to deal with this issue (e.g. by prohibiting any active trading by the new company until its conflicting name issue has been resolved).

2.10 **Section 15 – Memorandum of Incorporation, shareholder agreements and rules of company**

This section of the Bill allows the board to make rules, which will apply on an interim basis until the next general meeting of the company. The Bill does not state what the consequences will be in respect of any action taken in that interim period if the rules are not subsequently ratified. The rules are further required to be filed with the Commissioner, but the Bill is silent on what should be done with the filing if the rules are not subsequently ratified. The consequences for the company of any non-ratification of the interim rules should be clarified in the Bill.

Similarly, it is recommended that any rules made by the board of a company should not bind shareholders of the company (subsection 15(6)), until they have been approved as contemplated in subsection 15(4)(c)(ii). Therefore subsections 15(6)(a) and (b) should only apply once the rules have been ratified by an ordinary resolution.

Subsection 15(7) states that the shareholders of a company may enter into any agreement with one another concerning any matter relating to the company but any such agreement must be consistent with the Bill and the company's Memorandum of Incorporation and any provision of such agreement that is inconsistent with the Bill or the company's Memorandum of Incorporation is void to the extent of the inconsistency. This seems to be an unduly onerous provision and there does not seem to be any reason why a shareholders' agreement that is inconsistent with the Memorandum of Incorporation should be void to the extent of the inconsistency. It is common practice in South Africa to provide in shareholders' agreements that to the extent that shareholders' agreements are inconsistent with the constitution of the company, the shareholders' agreement shall prevail. The subsection should therefore be amended to cater for differences between shareholders' agreements and the company's Memorandum of Incorporation (i.e. shareholders' agreement to prevail), provided that the shareholders' agreement may not be in conflict with the Bill.

2.11 **Section 17 – Alterations, translations and consolidations of Memorandum of Incorporation**

Subsection 17(2) notes that the Companies Ombud can issue "an administrative order setting aside the notice of an alteration…" As noted above (item 1.2) this clearly sets out the role of the Companies Ombud as an Appeal Tribunal, not a consumer Ombud.

2.12 Section – 20 – Validity of company action

We would caution against any provisions in the Bill (e.g. subsection 20(6)) that might be interpreted to create strict liability i.e. faultless liability, on the part of directors or employees. This subsection should be amended to provide for actions to be based on fraud or gross negligence. Similarly, any liability for damages as contemplated in this subsection should be determined by normal delictual principles.

2.13 Section 21 – Pre-incorporation contracts

Section 21 provides that a person who enters into a pre-incorporation contract in the name of, or on behalf of a company not incorporated yet, incurs personal liability if the company is not subsequently incorporated or if the company rejects any part of the pre-incorporation contract. This may dissuade entrepreneurs from starting companies and from concluding pre-incorporation contracts. We recommended that the Bill be amended to state that such party shall incur personal liability only to the extent provided for in the pre-incorporation contract.

As noted above in item 2.1 on the definition of "agreement" the use of the word "purport" in this section conveys an incorrect sense of what the Bill sets out to achieve, and this word should also be deleted.

There are no time limits stipulated in subsection 21(2) within which a company should be incorporated for purposes of subsection 21(2)(a). Given the personal liability imposed under this section of the persons involved in the pre-incorporation agreements some maximum time for incorporation should be included.

It is suggested that for a company deemed regarded to have ratified an agreement or an action because of its failure to ratify or reject the agreement within a certain time (subsection 20(5)), it must at least have had knowledge of the particular agreement or action done in its stead. Upon a strict interpretation of the clause, any person can enter into an agreement on behalf of a company to be incorporated. It should be made an obligation on that person to inform the board of the incorporated company of the pre-incorporation agreement or action to enable the board of that company to consider the agreement within the stipulated three month period.

2.14 Section 22 – Reckless trading prohibited

Subsection 22(1)(b) of the Bill prohibits a company from trading under "*insolvent circumstances*". The term "insolvent circumstances" is not defined in the Bill, and it is unclear how it would relate to the solvency and liquidity tests referred to in Section 4. We suggest that a definition be provided for "insolvent circumstances" to clearly specify under what circumstances the subsection would be applicable.

2.15 Section 23 – Registered office

In subsection 23(2) the words "*conducting business*" should be changed to "carrying on business" to conform to the definition of "*external company*" in section1.

Subsection 23(2) further restricts the registration of external companies unless that foreign company has or is engaged in "*all or more*" of a list of 8 designated activities. It is highly unlikely that any foreign company would engage in "all" the listed activities, so presumably the section should read "one or more". However, even this new interpretation is open to question,

given the specific list of designated activities in the subsection (e.g. a foreign company holding a board meeting at say Sun City would have to register as an external company under subsection 23(2)(b), all non-resident of foreign account holders in banks would have to be registered as external companies under subsection 23(2)(c), and banks would have to ensure that their foreign international counterparties or correspondent banks are similarly registered in terms of subsection 23(2)(h)). Clarity is required on the exact intention of the drafters on this subsection.

The reference in subsection 23(4) to "subsection (2)(b)(ii)" should presumably read "subsection (**3**)(b)(ii)".

Subsection 23(1) requires an external company to register "within 20 business days…", but subsection 23(6) allows a 12 month window before any administrative action is taken for failing to so register. It is unclear why such a long period for non-compliance is provided for. At most this should be 20 business days.

2.16 **Section 24 – Form and standard for company records**

The Bill does not specify requirements for data to be stored electronically (subsection 24(1)(a)). Reference should be made to the ECT Act by including a clause stating that information stored in an electronic format should meet the requirements set out in ss15-17 of the ECT Act.

In subsection 24(1)(b) provision is made for records to be kept for "*a period of seven years, or any longer period of time…*". It is recommended that this period of 7 years be reduced to **5** years as required for accounting and tax records.

Subsection 24(4) notes certain details pertaining to directors. While subsection 24(4)(g) does make provision for "any prescribed information" it is nonetheless recommended that the identification details be explicitly cross-referred to the FICA requirements (e.g. including residential address).

2.17 **Section 27 – Financial year of company**

Subsection 27(6) indicates that if in a particular year, the financial year of a company ends on a Saturday, Sunday or public holiday, that financial year will be regarded to have ended on the next following business day. This implies that if a company's year end is 31 December and in a particular year that day falls on a Saturday, with Monday being a public holiday, the company's financial year end would end on the 2nd of January. This is clearly problematic, as operationally all systems cater for a hard month close. Furthermore, comparisons between financial years may be problematic since one financial year may contain 365 days and the next 367 (or even 368 in a leap year) etc. In a business such as banking where interest income is earned on weekends and public holidays, effective comparison between financial year ends would be lost. It is recommended that subsection 27(6) be deleted.

2.18 **Section 28 – Accounting records**

While the section enables "accurate and complete accounting records" to be kept in one of the official languages of the Republic, local accounting and financial reporting standards generally comply with international standards (e.g. see subsection 29(5)), and it is highly likely that the terminology required has not yet been developed in the 10 non-English languages. There may therefore be practical challenges in implementing this section.

2.19 **Section 29 – Financial statements**

Given the wide application of financial statements in this section, and the definition of such statements (as amended per our recommendation – see item 2.1 above), it may be necessary to further revise the definition of "*financial statements*" in section 1 of the Bill to include the words "**<u>that an actual or prospective creditor or holder of the company's securities, or the commission, panel or other regulatory authority, may reasonably be expected to rely on</u>**" and applicable to the whole definition of "*financial statements*".

The term "*may*" appears to provide the Minister with discretionary powers in terms of making regulations or not in subsection 29(4). Given the import of such regulations (accounting and financial reporting standards; alignment with IFRS) and the overall nature of the Bill that indicates that these regulations are mandatory it is recommended that the word "*may*" be replaced with "**<u>must</u>**".

2.20 **Section 30 – Annual financial statements**

Section 30 (3) provides for an "appeal tribunal" role to be fulfilled by the Companies Ombud, as noted previously.

2.21 **Section 31 – Access to financial statements or related information**

The proposed wide definition of "*financial statements*" creates difficulties in interpreting this clause, and it is recommended that this definition be amended (as noted above in item 2.1).

2.22 **Section 32 – Use of company name and registration number**

Subsection 32(3)(b) would seem to prohibit companies from trading under other names than those they are registered under (i.e. "…*to convey a false impression that the name is the name of a company.*"). Many large companies, especially banking groups that have to trade in a single company structure for capital efficiency purposes, use different divisional or product brand names to interact with the public and customers. These brands carry a substantial amount of goodwill and are well known, often relating to prior companies that have been merged of amalgamated. Within the banking sector, these different trading or brand names, which are different from the registered company name, also have to be approved by the Regulator (the Registrar of Banks). These brand names or trade marks would then also be appropriately registered to protect their exclusive use. It is recommended that this subsection be more clearly drafted in order to prevent the mischief at which it is intended, but to also allow a company to use its own registered brand names. It should be noted, again in the financial services sector where such practices are common, that all such brand names have to be referenced back to the company that owns them (e.g. "Wesbank, a division of First Rand Bank Limited, an authorised financial services provider").

It is recommended that the misrepresentation referred to in subsection 32(5) should be intentional or deliberate, especially in the light of the remedy provided for in subsection 32(6).

2.23 **Section 33 – Annual transparency and accountability report**

The heading of this section would appear not to be related to the content of the section (other than vague references to "prescribed information"). Clarity is required on the exact scope of the reports envisaged under this section.

2.24 Section 35 – Legal nature of company shares and requirement to have shareholders

Subsection 35(3)(b) would seem to be an error, as compliance with this subsection (i.e. that a company must at all times have at least 1 share held by a person not held or controlled by the other shareholders) precludes the existence of "wholly-owned subsidiaries". The intent of this subsection is unclear, and it is recommended that it be deleted.

2.25 Section 37 – Preferences, rights, limitations and other share terms

Subsection 37(5)(b) of the Bill indicates that a company's Memorandum of Incorporation may establish a particular class of shares, preferences, rights, limitations or other terms. This would include shares that are redeemable or convertible at the option of the company, the shareholder or any other person at any time or upon any specified contingency. The instruments are referred to as shares, but could, depending on the terms of the instrument, be debt instruments in terms of IFRS. Section 43, on the other hand, deals with debt instruments, which exclude promissory notes or loans. It is therefore possible that section 37 may define a certain instrument as a share, but section 43 defines it as a debt instrument. It is recommended that the terminology of these sections should be improved or harmonised, and that care is taken to ensure that these definitions of shares and debt instruments are consistent with IFRS.

2.26 Section 38 – Issuing shares

It is unclear in subsection 38(3)(b) whether the value that is returned should be the fair value on receipt of the consideration (plus interest as prescribed), or when the consideration is returned? The use of the term "*fair value of the consideration received*" would seem to indicate that the fair value should apply as at the time the consideration is returned (otherwise there would be no need to mention a fair value in this context, i.e. the actual consideration received would be returned). Perhaps the simplest solution would be to refer to "consideration paid, plus interest as prescribed". However, clarity is required.

2.27 Section 39 – Pre-emptive right to be offered and to subscribe shares

The heading to this section would appear to bear little or no relation to the content of the section.

2.28 Section 40 – Consideration for shares

This section refers on several occasions to holding shares "in escrow". It is unclear whether this concept as used in the section is applicable in local law, or whether the legal concept "in trust" should rather be used. (See also subsection 50(2)(b)(iii)).

If shares are issued pursuant to subsection 40(5) i.e. in return for a negotiable instrument that is not yet negotiable or for services to be rendered, they have to be issued and placed in escrow (or trust as noted above). If the instrument is not made negotiable or the services aren't rendered, the shares must be cancelled. Such cancellation should be made exempt from Uncertificated Securities Tax. Also, restrictions pertaining to shares issued in return for non-negotiable instruments e.g. voting rights, may not be exercised. This may prove problematic, for example in instances where one buys shares/debt with negotiability restrictions. It may also be a problem for asset-for-share transactions in terms of the Income Tax Act, where rollover relief is only provided (in the case of the acquisition of shares by a non-listed company in

return for shares therein) if at least 20% of the equity shares and voting rights are acquired in the non-listed company by the seller. Clarity is required.

It is not clear why transfers in terms of subsection 40(6)(d)(ii) can only be effected quarterly, especially in light of the mandatory provisions of subsection 40(6)(d)(iii).

2.29 **Section 41 – Shareholder approval for issuing shares in certain cases**

A special resolution is required in terms of subsection 41(b) for the issue of convertible shares to a related or inter-related person, a director, prescribed officer, or future director or prescribed officer. Notwithstanding subsection 6, it is difficult for any company to know at the time of the grant of the option if someone is a "future director/prescribed officer", or inter-related (see previous comment on difficulties relating to the determination of related persons). It is recommended that the concept of "future" be deleted, alternatively that the company should have explicit knowledge that the person is likely to be a director or prescribed officer at any time in the future.

2.30 **Section 42 – Options for subscription of securities**

Section 42 indicates that a decision by the board that the company may issue any options also constitutes the decision of the board to issue any authorized shares or other securities for which the options may be exercised. Options may take various forms – they may be settled with shares, i.e. fixed amount of cash for a fixed number of shares, net settled in shares, i.e. difference between strike price and final share price is settled net in shares, or settled net in cash, i.e. difference between strike price of option and final share price is settled net in cash. The section 42 requirements do not appear to be necessary where the terms of the option require settlement in cash (i.e. no securities are issued) [Note that the definition of securities in terms of the Securities Services Act does not include cash.]

2.31 **Section 43 – Securities other than shares**

The word "that" in subsection 43(2)(a) should be deleted.

Subsection 43(1)(a)(ii) excludes "*promissory notes*" from the definition of "*debt instrument*". It is unclear why this has been done in the Bill, as these legitimate debt instruments are not dealt with anywhere else in the Bill (other than in subsection 108(3)(b), in a non-related manner). Clarity is required, alternatively that this exclusion be deleted.

The Companies Bill requires annual financial statements to be prepared in accordance with IFRS. The definitions of shares and debt instruments in terms of IFRS may in many instances be contradictory to that of the Companies Bill, and alignment will be necessary.

2.32 **Section 44 – Financial assistance for subscription of securities**

Section 38(1) of the Companies Act, 1973 applies to financial assistance provided "directly or indirectly", whereas section 44 of the Bill does not do so expressly. The qualifications "**directly or indirectly**" should be included in section 44(2) after the words "*provide financial assistance*".

In terms of subsection 44(2) the prohibition applies to financial assistance provided to fund the purchase or subscription of shares in "*the company or a related or inter-related company*". Read together with the definitions of "related" and "inter-related" in section 1 of the Bill, this means the prohibition will apply to financial assistance provided to fund the purchase or subscription

of shares in the company, its holding company, its subsidiaries and sister companies. Subsection 38(1) of the Companies Act, 1973 currently only applies to the purchase or subscription of shares in the company or its holding company, i.e. the new prohibition will accordingly be applied too broadly. It is recommended that the reference to "*or a related or inter-related company*" be deleted and substitute with "**or its holding company**".

Subsection 44(2) should presumably read "*to the extent that the Memorandum of Incorporation does not provide otherwise*".

It is unclear why financial assistance is only permissible if authorised within the previous 2 years by a special resolution (subsection 44(3)(a)(ii)? It is recommended that the 2 year period restriction be deleted.

The word "**financial**" should be inserted before the word "*assistance*" in subsection 44(3)(a)(ii) for purposes of consistency.

Subsection 44(6) refers to subsection 77(3)(e)(iv) of the Bill. Subsection 77(3)(e)(iv) is however not consistent with section 44 in that it refers to "*the provision of financial assistance ...for the acquisition of securities of the company*" and does not refer to related or inter-related companies, as section 44 does. Subsection 77(3)(e)(iv) should be amended accordingly. (This comment does not take away from the comment above - both section 44 and subsection 77(3)(e)(iv) should refer to "the company or its holding company".)

2.33 Section 45 – Loans or other financial assistance to directors

This section applies not only to loans or financial assistance to directors or other officers or related parties, but also to "*a related or inter-related company or corporation*" (subsection 45(2)). However, subsection 45(3)(b)(ii) requires all loans or financial assistance under the section to be "fair and reasonable to the company". This subsection unnecessarily restricts the company's rights to contractual freedom, and introduces a concept ("fair and reasonable") that is largely foreign in local law of contract. Furthermore, there may be particular group circumstances that dictate that any such inter-group transactions are not "fair and reasonable" to the company that provides the assistance, in order for the greater group to benefit from that set of circumstances. It is recommended that subsection 45(3)(b)(ii) be deleted.

In terms of section 45(5)(a), certain disclosure requirements are triggered when specified loans directors and other prescribed officials exceed 0.1% of the company's "net worth" - this is not defined and could be difficult and costly to determine. Is section 45 subject to section 44 i.e. if a loan is to a director for a share purchase, does notice to shareholders and trade unions still have to be given under 45(5)? Also, why is it possible to provide financial assistance to a member of a related company (45(2)), but not to a member of that company providing the assistance (unless the member is related)? It is not clear if these are the only (non-ordinary course) loans a company may make, or if these specific loans only are subject to the requirements of section 45. The subsection is obviously also particularly important to banks as lending institutions. It is recommended that the notice requirement in this subsection should be triggered by the company failing to meet its solvency and liquidity requirements, rather than loan size as a percentage of a difficult-to-determine valuation.

2.34 Section 48 – Company or subsidiary acquiring company's shares

Section 48 indicates that any subsidiary of a company may acquire shares in that company (to a pre-defined limit), but that no voting rights attaching to those shares may be exercised while the shares are held by the subsidiary. Also, it remains a subsidiary of the company whose shares it holds. At first glance it would appear understandable that a subsidiary should not be permitted to vote on shares that it holds in its own holding company. However, consider the following scenario:

> Company A owns 100% of Company B. Company A has 100 shares in issue, 50 of which are owned by Company X and the rest by a number of other shareholders. Company X does not control Company A. Assume that Company B purchases 10 shares in Company A. Does this imply that:
>
> - Company X continues to only exercise a voting capacity on 50 out of 100 shares in company A?; or
> - Does Company X now control Group A (company A) by virtue of 50 votes out of a pool of 90 votes = 56% due to the fact that votes on 10 shares are not able to be exercised?

This may result in control by a company over another where control was not an objective. This may result in severe accounting and tax implications.

Secondly, this could result in Company X having to account for Company A as an acquisition and subsequent disposal each time Company B buys and sells shares in Company A (if regularly performed).

We suggest that the reference to "<u>10% of, in aggregate of the number of issued shares</u>" be deleted as the rational is not clear, and it could introduce unintended consequences.

In respect of a company buying back its own shares, the Companies Act, 1973 requires that shares bought back must be cancelled as "issued shares" and restored to "authorised but not issued shares". It is recommended that such an explicit provision be retained in the new Bill.

2.35 Section 55 – Liability relating to uncertificated securities

As noted previously it is recommended that faultless or strict statutory liability should not be provided for in the Bill, but rather that any person who acted reasonably, i.e. without fault (negligence or intent) should not incur liability. If the legislator's intention here is to only hold intentional unlawful conduct liable, then this should be clearly specified.

2.36 Section 56 – Beneficial interest in securities

This section provides for the identification of certain shareholders including those with a beneficial interest in securities. However, it focuses only on the immediate shareholders or 1 level up for nominee holdings. This is not consistent with the "know-your-client" regime imposed under FICA and international anti-money laundering standards. These require certain institutions (called "accountable institutions" in FICA) to pierce the corporate veil to identify the ultimate <u>**individuals**</u> who have a beneficial interest in the securities. It is recommended that the new Companies Bill support this statutory onus under FICA, by requiring companies to declare all <u>**individuals**</u> who have any beneficial interest, irrespective of through how many layers of corporate intermediary.

Where a trust or company holds shares in a public company and another person gives instructions to the trustees/directors who are accustomed to act on that other person's behalf, that other person is deemed to be the beneficial shareholder. Previously nominees were deemed members (but only a limited category of nominees was provided for). This may have far-reaching tax ramifications for the company (as well as for its shareholders) e.g. a local company pays dividends to a local trust with a non-resident deemed beneficial owner. When dividend withholding tax is enacted, the company would have to enquire as to ultimate beneficiary to determine the withholding requirement. The same applies to the provision deeming a company which controls another (subsection 56(2)(e)) to be the beneficial owner of shares in a public company e.g. Banking group XYZ owns Bank SA which owns shares in a public company. The banking group XYZ is deemed to be the beneficial owner which may have unintended tax (and other) consequences. It is therefore recommended that Section 56 be amended to explicitly state that the deeming provisions apply for purposes of the Companies Bill only.

2.37 **Section 57 – Interpretation and restricted application of Part**

We recommend that the concessions contained in the Act for companies of which all the shareholders are also directors, should also be applied where those shareholders are juristic persons and have specifically appointed and authorised an individual to serve as a director on the relevant company. There are a significant number of such companies in existence, e.g. special purpose vehicles within the financial sector, that serve legitimate business purposes. We believe that such an extension would not be detrimental to proper corporate governance processes as proposed in the Bill, but it would greatly simplify the required corporate and governance processes for these companies. Consequential drafting revisions would be necessary for this de facto simplification, e.g. of the subsection 57(4) provisions. Alternatively, a different solution could be not to expressly legislate for this particular event, but to enable a company to provide therefore in its Memorandum of Incorporation, if it so chooses.

It is recommended that subsection 57(1) be amended by inserting the word "**unconditionally**" before the words "*exercise any voting rights*".

2.38 **Section 58 – Shareholder right to be represented by proxy**

Subsection 58(2) read with subsection 58(8) makes it unclear what the situation is if proxies are given for more than one meeting - does subsection 58(2)(b)(i) (proxies valid for one year) override subsection 58(8)(d) (proxies valid until end of meeting)? We recommend that the provisions be aligned and that a proxy be valid until the end of a meeting.

2.39 **Section 60 – Shareholders acting other than at meeting**

It is not clear from the section what would happen if not everyone wants to, or is able to, vote "*in writing*" as provided for.

Subsection 60(5) provides that any business of a company that is required to be conducted at an annual general meeting may not be conducted in the manner contemplated in the section. This seems unnecessarily restrictive, and an alternative to the holding of an AGM should be provided in the same way as the Companies Act, 1973 allows an AGM to occur other than at a meeting.

2.40 **Section 61 – Shareholder meetings**

This section contains several references to the role of the Companies Ombud that are more appropriately dealt with by an "appeal tribunal" or other administrative body , as noted above.

Subsection 61(8)(c) sets out the minimum business to be conducted at an AGM. This includes the appointment of the audit committee. From a governance perspective this is wrong. The audit committee is a committee of the board and should not be subject to shareholder appointment. It removes flexibility for the board to operate between meetings and the committee is accountable to the board. In addition, the board is best placed to elect the audit committee from its knowledge of the business and the director's abilities. Subsection 61(8)(c)(c(ii) should be deleted. Similar provisions in subsection 94(2) should also be deleted.

The obligation imposed by subsection 61(10) may be impossible for public companies having thousands of shareholders to comply with. It will not be possible to cater for the needs of every shareholder to participate electronically (even if such provision must only be "reasonably accessible"). Perhaps this subsection should be amended to provide that a <u>majority</u> of shareholders (in number and value) should have reasonable access.

We recommend that subsection 61(13) relating to that the company's obligation to compensate should only be triggered if the application concerned is successful.

2.41 **Section 62 – Notice of meetings**

The definition of "*business day*" is not unusual as is the description in subsection 5 (3). However, what is of concern is the use of the term in relation to the timing of circulation of notices. Previously the days required for notice were just "days" and not business days which take into account public holidays and weekends. The new use of business days in this context is onerous as it has brought forward the required posting date for shareholder notices, for no obvious benefit. This is especially the case in South Africa with the number of public holidays in April/May which is the usual time for posting/counting days for companies with December year ends. It is recommended that the reference to "*business day*" in section 62 be replaced with "<u>**day**</u>", and that the number of days for calling of meetings be retained as set out in Companies Act, 1973.

Subsection 62(4) combines both "failure to give notice" and "defective notice", including the remedies in each case. This could result in confusing interpretations of the remedies. It is recommended that the subsection be amended to provide for each situation separately, specifically:

- Subsections 62(4)(b) and (c) for failure to provide notice, and
- Subsections 62(4)(a) and (d) for defective notice.

2.42 **Section 63 – Conduct of meetings**

Subsection 63(5) indicates that an abstention 'or other failure' by a person present at a meeting to exercise any vote must be regarded as being an exercise of voting rights in opposition. This is not necessarily true. While it is an accepted practice that an abstention (which is a conscious choice and so recorded) is effectively a vote against a resolution, shareholders should have the right to attend a meeting without casting a vote, i.e. not casting a vote is different to abstaining from that vote. It is therefore recommended that the word "<u>or other failure</u>" be deleted.

2.43 Section 64 – Meeting quoram and adjournment

The requirements of subsection 64(3)(a) could be particularly onerous if there were only 3 shareholders, one of whom owned say only 1 share or a very small percentage. Perhaps a greater threshold should be specified for this subsection to apply, e.g. a minimum of 10 shareholders (i.e. 3 of the 10 shareholders would have to be present).

2.44 Section 65 – Shareholder resolutions

The provisions of subsection 65(3), while understandable in the context of good intentions, also need to be considered from the perspective of perverse or unintended consequences. These provisions may be open to abuse by disgruntled or vexatious shareholders that totally dominate a shareholders' meeting, causing a breakdown in good corporate governance processes (e.g. the meeting terminates in chaos, without the rest of the agenda being dealt with). This is particular relevant in the case of the banking sector, where disaffected clients become "1 share shareholders" and totally disrupt the shareholders' meeting in an attempt to air their grievances. It is recommended that the subsection be amended to allow that a company or its board may refuse to submit such a resolution to the shareholders for consideration on the basis that it is vexatious, frivolous or patently without merit, in case of which the aggrieved shareholder may apply to the Ombud/appeal tribunal or the courts to have such resolution submitted for consideration. Similar processes existing in law to have certain person declared "vexatious or frivolous litigants".

Subsection 65(4)(b) refers to a "*reasonably alert shareholder*" – there is no understanding of exactly what this condition is or should be. It is recommended that the words "reasonably alert" be deleted.

2.45 Section 66 – Board, directors and prescribed officers

Subsection 66(4)(b) provides that only 50% of the directors need to be elected by shareholders. This is a retrospective governance move away from the English model of having all directors approved by shareholders to the US system where effectively there is no shareholder approval. The ability to appoint any director that is not somehow subject to shareholder approval should be deleted in its entirety or provision made for all director appointments to be subject to shareholder approval. This must provide for board appointments between general meetings after which a director must either retire or stand for re-election at the general meeting directly after his appointment. It is therefore recommended that this subsection be deleted.

Subsection 66(10) allows for the payment of fees to directors only if '*approved by special resolution*', however in our view there is absolutely no basis for the increased approval hurdle. There are now sufficient provisions in the Bill relating to director liability and good corporate governance. The requirement to only be able to pay after a special resolution is passed is unduly onerous and it is recommended that the reference to "special" resolution be deleted and replaced with ordinary resolution.

2.46 Section 69 – Ineligibility and disqualification of persons to be director or prescribed officer.

This section introduces a "deeming" provision that extends the liability of directors to other (non-director) members of the audit committee or other board committees. This is a serious provision and is likely to preclude many skilled employees of a company from participating in a directors' committee,

to the detriment of those committees. It is recommended that this section be rewritten to exclude this "deeming" provision, and to restrict directors' functions and liability to appointed or elected directors.

It is unclear how the Commission will be able to establish and populate the "public register of persons who are disqualified from serving as director," nor how such highly sensitive information will be kept accurate and up-to-date. While the intent of the register is clear, the actual implementation will be extremely difficult.

2.47 **Section 70 – Vacancies on board**

It would appear from this section that the board may not be able to fill an interim elected vacancy on the board until the next AGM, or by arranging a special general meeting or poll. This severely restricts the ongoing functional capability of boards, and increases the costs unnecessarily. It is recommended that the section be amended by deleting subsection 70(3)(b) and replacing it with a provision enabling the board to fill any such vacancies, which appointments must be ratified (or otherwise) at the next AGM.

2.48 **Section 71 – Removal of directors**

This section contains further references to duties of the Companies Ombud that are more appropriate to an appeal tribunal or other administrative body.

Subsection 71(1) provides for the removal of directors by ordinary shareholders' resolution. It is unclear whether this subsection is subject to section 60 or not, i.e. can this resolution be obtained in writing without the need for a meeting? If so it should be explicitly stated, especially since the election of directors is specifically referenced in section 60, but their removal is not. Il is recommended that the following text be inserted before "*subject to subsection 2*": "**or by written polling of all of the shareholders entitled to exercise voting rights in relation to the election of a director**".

The rights given to shareholders in terms of subsection 71(3) may be abused by disgruntled "1 share shareholders", as noted in the comments on section 65 above. It is recommended that the company be entitled to refuse to consider such shareholder requests where they are patently vexatious or frivolous, or without merit.

2.49 **Sections 75 – 78**

These sections all provide for certain persons to be "deemed" directors. As noted above this provision will negatively impact the willingness of employees to serve on any of the directors' committees, and the sections should be rewritten to exclude such a "deeming" provision.

2.50 **Section 76 – Standard of directors conduct**

As the Bill currently stands it is unclear whether or not the directors' conduct and duties set out in this section would "override" the provisions of any other law (for example the Banks Act, 1990) dealing with similar directors' duties. The implication of subsection 5(4) referred to above is that the Companies Bill would prevail in the event of a conflict between the Companies Bill and the Banks Act. It is therefore important that recommended amendment to provide for the Banks Act to prevail be implemented.

2.51 **Section 77 – Liability of directors and prescribed officers**

As noted previously we are opposed to any provision which may be interpreted to impose strict (faultless) liability on a director (e.g. subsection 77(3)). We believe that the courts should be allowed to determine sufficient guidelines in relation to a director's duty of care or instances in which such director may be seen to be negligent, which should serve as proper protection of the interests of stakeholders and the company itself. In this regard it is unclear whether the provision at the end of sub-section 77(3)(d)(ii) – "despite knowing that the statement was false, misleading or untrue" – applies only to subsection 77(3)(d)(ii) or the whole of subsection 77(3)(d). We recommend that it be clearly drafted to cover the whole subsection (i.e. parts (i) and (ii)).

In the light of the reasonably wide definition of "*material*", it is recommended that the untrue statement mentioned in sub-section 77(3)(d)(ii)(aa) should be material.

Subsection 77(7) should be amended by including the words "**and it came to the knowledge of the other party**" after the word "*liability*" at the end of the sentence.

The current wording of subsection 77(10) would seem to imply that if a director has reason to apprehend that a claim may be brought against him in which it is alleged that he is liable on the basis of wilful misconduct or wilful breach of trust, he will be barred from applying for relief to a court. Obviously such allegations do not mean that the director acted as alleged, and such allegations should not preclude the director from approaching the court. It is recommended that the wording should be amended in order to prohibit a court from granting the relief if wilful misconduct or wilful breach of trust can be attributed to the director. This would be achieved by deleting the words "*other than for wilful misconduct or wilful breach of trust*" and re-inserting them after the words "*grant relief to the director …* " in the second last line of the subsection. We assume that this would correlate with the intent of the Bill.

2.52 **Section 78 – Indemnification and directors' insurance**

Reference to "director" in subsection 78 (1) should be amended to also include "**former directors**", as a director can be held liable after termination of his term, for actions and decisions whilst in office.

Subsection 78(6)(b) could be interpreted as restricting the company from taking out any other insurance to mitigate its risks. It is recommended that this subsection be clarified (beyond the provisions in the Memorandum to Incorporation) to ensure that the subsection should apply without any restriction on insurance that a company would be able to obtain in the normal course of business.

2.53 **Section 79 – Winding-up of insolvent companies**

The reference to "*interested person*" in subsection 79(3) is unclear, and should be defined to ensure legal certainty in this context.

2.54 **Section 81 – Winding-up of solvent companies by court order**

Subsection 81(1)(d)(ii) refers on to the situation where directors' terms have expired. It is unclear why all the other reasons for a vacancy on the board, and on which there is deadlock, should not also be dealt with in a similar manner. It is therefore recommended that the words "*have expired*" be

replaced with "**whose terms of office have terminated for whatever reason**."

2.55 **Section 82 – Dissolution of companies and removal from register**

It is unclear how the Commission will identify, attach and hold in trust all the assets that may be relevant for all the deregistered companies, nor even why it should want to be involved in any such activities. Presumably this would also represent net assets after all outstanding liabilities have been settled.

2.56 **Section 83 – Effect of removal of company from register**

This section provides for certain actions to be taken, or liability to remain, indefinitely. This could involve an inordinate amount of record keeping for the Commission. It is recommended that a definite time limit, e.g. 5 years after the company was deregistered, be included in the Bill.

2.57 **Section 84 – Application of Chapter**

This section includes a role for the Companies Ombud more suited to an appeal tribunal.

2.58 **Section 86 – Mandatory appointment of secretary; Section 89 – Resignation or removal of company secretary**

There do not appear to be any criteria relating to the disqualification for the appointment of a company secretary. Perhaps consideration should be given to including a provision similar to section 268F of the Companies Act, 1973, and that for example section 162 of the Bill should apply *mutatis mutandis* to secretaries.

2.59 **Section 87 – Juristic person or partnership may be appointed company secretary**

The general provision of this section is welcomed. However, it would be unduly restrictive and costly to require that "*every employee, or partner and employee of that partnership*" should have to comply with the specific provisions as stipulated. This requirement should only be applicable to directors, members, partners or employees directly involved in the affairs of the company for which the company secretary functions are being performed.

2.60 **Section 88 – Duties of company secretary**

The duties of the company secretary under subsection 88(2)(b) ("*making the directors aware of any law relevant to or affecting the company*") are noted. However, subsection 60A of the Banks Act, No 94 of 1990 establishes a compliance function for banks and the appointment of a designated compliance officer is mandatory. The compliance function within a bank ensures that the institution complies with all relevant legislation applicable to it, apart from the Companies Act which is in general the responsibility of the company secretary. There is therefore potentially overlapping or conflicting legislation in this regard. It is recommended that subsection 88(2)(b) be amended to make provision for these duties to be ascribed to the compliance officer in terms of the Banks Act.

2.61 **Section 89 – Resignation or removal of company secretary**

It is unclear why, of all the designated or prescribed corporate governance officials, provision should be made in the Bill (subsection 89(2)) for the company secretary who is removed from office to include an explanatory statement in the company's annual financial statements. There are sufficient

other channels for the company secretary, as with other officials, to report any concerns or have any issues addressed. It is recommended that the whole section be deleted.

2.62 **Section 93 – Rights and restricted functions**

It is unclear why any auditor, appointed by a company, should have to approach a court to enforce its right to access certain documentation or information in order for it to discharge its duties. In such a case where trust between the parties appears not to exist the auditor should probably resign and report as such to the Commission and other relevant regulatory bodies.

2.63 **Section 94 – Audit Committees**

This section excludes banks from certain of its provisions, as the Banks Act, 1990 also deals with audit committees (section 64 of that Act). However, it is unclear why banks are not excluded from subsection 94(4), as this subsection overlaps with subsection 64 of the Banks Act in terms of setting parameters for the members of the audit committee. It is recommended that subsection 94(1)(a) be amended to include subsection **4** of the Banks Act as well.

Alternatively, subsection 94(4)(b) is extremely restrictive, as it effectively imposes a "restraint of trade" on potential directors/members of the audit committee with the requisite experience by imposing a minimum 3 year exclusion. It is recommended that this period be reduced to 1 year.

2.64 **Section 95 – Application and interpretation of Chapter**

This section defines a "compliance officer" purely in relation to a company's employee share scheme. However, the term and concept "compliance officer" is used more generally in other legislation (e.g. the Banks Act, 1990 (section 60A); the Financial Advisory and Intermediary Services Act, 2002 (section 17); the Financial Intelligence Centre Act, 2001 (section 43)) in relation to ensuring compliance with the whole Act (and other applicable legislation). The Bill's restrictive definition could result in confusion within companies, and for employee training and career pathing of "compliance officers". It is recommended that the Bill be amended to use another term than "compliance officer".

2.65 **Section 97 – Standards for qualifying employee share scheme**

This section determines the requirements for a share scheme to qualify as an "*employee share scheme*", which qualification is associated with certain exemptions (subsection 97(1)). However, as worded compliance is total and absolute, and makes no provision for technical or minor/immaterial non-compliance (e.g. a document is filed 1 or 2 days late). It is therefore recommended that such compliance obligations should be included in the rules or administration of the employee share scheme. Alternatively, if absolute compliance with the said section is required for a scheme to qualify as an employee share scheme, provision should be made for such technical non-compliance by amending subsection 97(1)(b) to read as follows:

> "(b) The compliance officer has **substantially** complied with the requirements of sub-section (2)."

References in subsection 97(1) to subsections 44(2)(c)(i) and 45(2)(c)(i) in the opening lines of this section should presumably read 44(3)(a)(i) and 45(3)(a)(i) respectively.

It is not clear from subsection 97(2)(c) who the documents referred to need to be "filed" with.

2.66 Section 112 – Proposals to dispose of all or greater part of assets or undertaking

The term "*dispose of*" in subsection 112(1) should be defined as it could (and has) lead to legal uncertainty. For example, if a property-owning company has as its main asset immovable property which it wishes to mortgage, and bearing in mind that there is the potential risk of the mortgagee (creditor) foreclosing on the property in a non-remedied default situation, does mortgaging of assets fall within the ambit of "dispose of"? Given below is a quote from commentary in Henochsberg on the Companies Act, 1973 which addresses this issue, but which is essentially only an opinion. Absolute clarification by way of a definition in the revised legislation will remove the difficulties in interpretation.

["Dispose.—It is submitted that, in the context, the word "dispose" has its ordinary meaning of "to part with" or "to get rid of" (as to the ordinary meaning of the word, see Cullinan Properties Ltd v Transvaal Board for the Development of Peri-Urban Areas 1978 (1) SA 282 (T) at 285-286) and accordingly the only disposal to which it is intended to refer is one which would have the effect of permanently depriving the company of its right to ownership of the assets involved. Thus, the grant of a right of first refusal to purchase is not within the section (Lindner v National Bakery (Pty) Ltd 1961 (1) SA 372 (O)). Neither is a pledge nor a cession in security (Alexander NO v Standard Merchant Bank Ltd 1978 (4) SA 730 (W)), notwithstanding, it is submitted, the divestitive effect of such a cession (see further the notes on s 342 vs. Costs, charges and expenses), having regard to the residual interest which the company retains in relation to the right ceded. It is submitted that passing a mortgage bond is not within the section (cf Advance Seed Co (Edms) Bpk v Marrok Plase (Edms) Bpk 1974 (4) SA 127 (C) at 132; and see L Hodes op cit in the General Note at F7-F9))."]

2.67 Section 114 – Proposals for scheme of arrangement

It is unclear how the company would be able to effect "an expropriation of securities from the holders" (subsection 114(1)(c)).

It is unclear who the "*offeror*" is in subsection 114(2), and this person should be clearly defined in the context.

It is recommended that subsection 114(2)(b)(ii) be deleted, as this criterion inherently included in subsection 114(2)(b)(i).

It is recommended that the words "**and creditors**" be inserted after the words "*holders of the company's securities*" in subsection 114(3).

2.68 Section 117 – Definitions applicable to this Part, Part C and Takeover Regulations

In the definition of "securities in subsection117(1)(j) the word **"unconditional**" should be in relation to the right to vote (subsection (i)) and to convert (subsection (ii)).

It is also unclear why the definition of "*Executive Director*" in included in this section, as the term is not used at all in the whole Chapter.

2.69 Section 119 – Panel regulation of affected transactions

The reference to "subsection (4)(b)" in subsection (5) should presumably read "subsection (4)(c)".

In terms of subsection 119(1) the Takeover Panel must disregard the commercial advantages or disadvantages of any transaction or proposed transaction or offer. It would therefore appear that the focus of the Panel is purely administrative to ensure fair treatment of all security holders and an adequate provision of relevant information. Is the expectation that the commercial aspects would be left to the Competition Commission to decide? Clarity is required.

2.70 Section 122 – Required disclosure concerning certain share transactions

Subsection 122(2)(b)(ii) refers to "*person who has acted in concert with any other person*". This is a wide-ranging criterion (e.g. what if two companies acted in concert a long time ago and have since gone their separate ways?) and it is recommended that its application be restricted to a relevant time period, e.g. "**<u>in the past year</u>**".

Subsection 122(3)(b) does not stipulate how other shareholders should be informed. Would a SENS announcement be sufficient or would a written letter/email suffice? Clarity is required.

2.71 Section 123 – Mandatory offers

The "*prescribed percentage*" is set at a maximum of 35% (subsection 123(5)). The section requires that one has to make a written offer the moment one's shareholding goes over this level. The intention of the <u>prescribed percentage</u> is unclear and should be re-visited as it could have unintended consequences.

2.72 Section 124 – Compulsory acquisitions and squeeze out

Subsection 124(2) does not give grounds for a court on which to rule or grant such an order. It is recommended that similar provisions to subsection 124(3)(b) i.e., fair and reasonable, just and equitable be included.

Subsection 124(4)(a) does not specify a time limit within which such notice must be sent to the relevant shareholders. It is recommended that the provision in subsection 440K(3) of the current Companies Act, 1973 that notice must be given within a month of the 90% threshold being passed, should be included (i.e. insert "**<u>within a month of acceptance of an offer</u>**" after "*the offeror must*").

2.73 Section 125 – Comparable and partial offers

In subsection 125(1)(a) replace the words "*mean*" with "**<u>means</u>**", and "*entitle*" with "**<u>entitles</u>**".

2.74 Section 127 – Prohibited dealings before and during an offer

The realities of issues such as BEE in the South African landscape necessitate special arrangements being made (provided these are duly disclosed) in order to enable offers to proceed. The Bill should not be prohibiting such transactions, and it is recommended that subsection 127(1) be reviewed to facilitate such transactions (e.g. as per the dti transformation Codes of Practice).

2.75 Section 128 – Application and definitions applicable to Chapter

It is unclear whether the definition of "*creditor*" in subsection 128(1)(e) includes contingent creditors, e.g. those who hold guarantees or suretyships from the company. It is recommended that this be clarified by including the

words "**or contingent arrangement, such as a guarantee or suretyship**" after the words "*under any arrangement*".

Subsection 128(1)(f)(i) deals with two criteria, namely the inability to pay debts, and liabilities exceeding assets, in the same section (linked with "and", i.e. both must apply at the same time). However, these two concepts are separated by an "or" when a potential situation is considered over the next 6 months (subsections (ii) and (iii)). It is recommended that subsection 128(1)(f)(i) be split into two subsections, with either (i.e. "or") being applicable for consistency of approach.

2.76 **Section 129 – Company resolution to begin business rescue proceedings**

Subsection 129(3)(b) provides for the company to appoint the supervisor. Please note that there are certain banks that feel strongly that, as with existing procedures to appoint a liquidator, the creditors should have the right to appoint the supervisor given their (generally significant) claims in relation to those of other stakeholders.

2.77 **Section 130 – Objections to company resolution**

Subsection 130(5)(c)(i) should be amended by inserting the words "**and thereby commencing the winding-up of the company**" at the end of the sentence to ensure certainty of the legal process.

Section 130(5)(c)(ii) refers only to the inability to pay debts, and not the other criterion for triggering business rescue (liabilities exceeding assets). It is recommended that the words "*would be unlikely to pay all of its debts as they become due and payable*" with "**is financially distressed**".

This section does not provide for the date of the concursus creditorum in the event that business rescue proceedings are converted to liquidation proceedings. It should be stipulated that the concursus creditorum, or winding-up process, comes into being when the court makes an order in terms of section 130(5), as the date of commencement of the winding-up is of considerable importance.

2.78 **Section 133 – General moratorium on legal proceedings against company**

It is recommended that a new subsection 130(1)(f) be inserted for legal certainty:

"**f) in respect of agreements to which Section 35A and Section 35B of the Insolvency Act, 1936 (Act No. 24 of 1936) would apply in a liquidation**."

Substitute the words "*a company*" in subsection 133(2) line 1 with "**the company**".

2.79 **Section 134 – Protection of property interests**

The first subsection should be numbered "**1**".

As presently worded the section refers to "*dispose of*", which has an unwarranted wide application over certain forms of security which would be affected not only by a disposal. Creditors obtain the benefits of security both from the disposal of secured assets and from their realisation. It is therefore recommended that the word "*dispose of*" be replaced with "**dispose of or to realise**", and "*disposal*" with "**disposal or realisation**".

2.80 **Section 135 – Post-commencement finance**

The clear understanding of the preferences accorded to any post-commencement finance is critical for any business rescue to be able to obtain such additional finance, given its already-financially distressed conditions. Subsection 135(3) indicates that such post-commencement finance will be ranked in preference "*in the order in which they were incurred*" – presumably this refers to dated and time. It is unclear how this information will be made transparent and managed to ensure that all post-commencement financiers are enabled to make informed decisions. Furthermore, it is not totally clear from subsection 135(3)(b) whether the description "*all unsecured claims against the company*" refers to only pre-commencement, or pre- plus post-commencement (i.e. all), as not all post-commencement finance will be secured (per subsection 135(2)(a)). Clarity is required on this extremely important provision.

2.81 **Section 136 – Effect of business rescue on employees and contracts**

The enabling of the supervisor, during any business rescue proceedings, to "cancel or suspend entirely, partially or conditionally any provision of any agreement …" (subsection 136(2)) is a cause for concern, as it introduces significant but unquantifiable risk into every contract, and undermines the whole contractual regime. It is recommended that this clause be amended to only encompass "suspend", on condition that the contracting counterparty so agrees. It is also unclear what would happen to any conditions that have been cancelled, once the business rescue process terminates (one way or the other).

Subsection 136(2) refers to subsections 35A and B of the Insolvency Act, 1936. It should be explicitly stated that the application of these 2 Insolvency Act sections apply despite there not being formal sequestration or insolvency proceedings, and that such application does not in any way imply or deem that the company is now in liquidation and subject to the Insolvency Act. However, there may be alternative interpretations that could mean that all of the transactions and agreements contemplated in these sections of the Insolvency Act would be subject to the supervisor's power to cancel or suspend, entirely or partially, any provisions of these agreements, and in the case of transactions governed by an ISDA Agreement, for instance, the counterparty could be prevented from exercising any of its termination rights, while the supervisor has the power to cancel or suspend any provisions of the agreement. This would destroy the protections afforded by these sections of the Insolvency Act.

If the intention of the wording in subsection 136(2) is that sections 35A and 35B should apply upon the commencement of business recovery proceedings, then this should be clarified. However, if this is the case, given the intention of the business recovery proceedings and the difference between this and a liquidation, thought should be given as to whether or not automatic termination of unperformed rights and obligations as contemplated in section 35B (as opposed to the right to terminate afforded by section 35A) would be the best way of dealing with this. It may be better to protect the counterparty's right to exercise its contractual termination rights under the agreements contemplated in section 35B, rather than a statutory automatic termination. As a comparison, under the United States Bankruptcy Code, "swap agreements" are specifically exempt from the automatic stay of proceedings in Chapter 11 and there is express protection for the exercise of contractual rights to liquidate, terminate or accelerate one or more "swap

agreements" and net or offset termination values and payment amounts under such "swap agreements". Perhaps a similar approach could be considered, in which case amend the subsection to read: "**Despite any provision of an agreement to the contrary, during business rescue proceedings, the supervisor may suspend entirely or conditionally any agreement with unperformed contractual obligations due by the company at the commencement of the business rescue period, other than an agreement of employment, provided that any reciprocal counter-obligation of any other party to the agreement is also suspended; provided further that nothing in this Act will have the effect in any way of altering or impeding the operation of any transaction or master agreement under Section 35A and Section 35B of the Insolvency Act, 1936 (Act No. 24 of 1936).**"

2.82 **Section 137 – Effect on shareholders and directors**

Subsection 138(2)(d) should equally also relieve directors from their duties under common law. This is especially pertinent as sections 76 and 77 do not necessarily codify common law duties of the directors. It is recommended that the following words be inserted after "*s77*": "**or any other duties that exist in law**".

2.83 **Section 138 – Qualifications of supervisors**

It is recommended that the list of qualifications for the supervisor in subsection 138(1) also included demonstrable legal, financial and business skills and experience.

It is unclear why only one person or association is contemplated in subsection 138(2) - substitute "*one person or association*" with "**one or more recognised professional or industry bodies**".

2.84 **Section 140 - General powers and duties of supervisors**

The supervisor's power to summarily dismiss any person in management (subsection 140(1)(c)(i)) may have Labour Relations Act and other contractual consequences. This section should either be deleted, or amended to include compliance with established labour relations processes and contractual obligations.

Insert the words "**wilfulness and/or**" before "*gross negligence*" in subsection 140(2)(c)(ii) to include the concept of wilfulness.

2.85 **Section 141 – Investigation of affairs of company**

This section contains a perverse impact on the role of the supervisor – he is appointed at what is likely to be a lucrative salary (which enjoys payment preference in terms of subsection 135 (3) of the Bill), but will have to "terminate" his own employment if at any stage he concludes that the business rescue process is likely to fail. It would be very tempting for the supervisor not to come to this conclusion, or to set standards for success that ensure his continued employment. Perhaps some independent, regular review of the business rescue process would be more appropriate.

2.86 **Section 143 – Remuneration of supervisor**

It is unclear what is meant by "**egregiously** unreasonable" in subsection 143(4)(b). This word is also not "plain language".

2.87 **Section 145 – Participation by creditors**

It is unclear in subsection 145(4)(b) what is meant by "subordinated in a liquidation", and perhaps this should be more clearly defined. Similarly, it is unclear where any preference shareholders would rank, and how they would be included in the process.

2.88 **Section 147 – First meeting of creditors**

This section, and section 148, require the supervisor to inform creditors and employees within 10 days whether the business rescue has a reasonable chance of success. While one can understand the urgency of the matter it may be impossible for such an informed position to be developed within the 10 business days, especially for bigger organisations. It is also unclear what the sanction is on the supervisor if he/she does not comply with this requirement.

2.89 **Section 152 – Consideration of business rescue plan**

The decision in subsection 152(2) should be supported by a majority of independent creditors i.e. those without other (potentially conflicting) interests. The following amendments are therefore proposed for this subsection:

"(2) In a vote called in terms of subsection (1)(e), the proposed business rescue plan will be approved on a preliminary basis if:

~~(a)~~ it was supported by the holders of more than ~~75~~ 50% of the **independen**t creditors' voting interests that were voted; ~~and~~

~~(b) the votes in support of the the proposed planincluded at least 50% of the independent creditors' voting interests, if any, that were voted.~~

2.90 **Section 153 – Failure to adopt business rescue plan.**

It is unclear what "**egregiously** irrational" in subsections 153(1)(a)(ii) or 153(1)(b)(i)(bb) means. The term is also not "plain language".

2.91 **Section 154 – Discharge of debts and claims**

It is presumed that this section and the reference to the business recue plan being "implemented in accordance with its terms and condition", or "implemented in accordance with this Chapter", would relate to the success of the business rescue. Under these circumstances it could be reasonable for a creditor to lose its rights as agreed under the plan.

However, if the rescue plan fails and the company moves into liquidation, then all creditors should be entitled to their full rights as they were immediately before the business rescue process was initiated. It is recommended that this section be amended to clearly preserve the creditors' original rights in the event of the rescue plan failing.

2.92 **Section 155 – Compromise between company and creditors**

Subsection 155(6) makes provision for the proposal to be adopted by the creditors, "*or the members of the relevant class of creditors*" – it is unclear under what conditions the "or" would be triggered, nor how the different classes of creditors would be determined or weighted relative to each other. Similarly the subsection requires support by "*a majority in number, representing at least 75%in value of the creditors or class*" – it is unclear what would happen if the creditor classes voted differently in relation to this support threshold. Clarity is required.

2.93 **Section 156 – Alternative procedures for addressing complaints or securing rights; Section 158 – Remedies to promote purpose of Act; Section 160 – Disputes concerning reservation or registration of company names.**

These sections imply a role for the new Companies Ombud more aligned to a tribunal than an Ombud, as noted previously.

2.94 **Section 159 – Protection of whistle-blowers**

It would be inappropriate for the Bill to attempt to regulate contractual or other common law obligations not expressly stipulated in the Act. It is therefore recommended that the expression "*legal obligation*" in subsection 159(3)(b)(ii) be amended to "***statutory*** *obligation*".

Subsection 159(7) is only applicable to public companies. It is recommended that this section be amended to also include state-owned enterprises.

2.95 **Section 162 – Application to declare director delinquent or under probation**

Section 162(5) states that the "court must make an order…" This statutory imposition interferes with the independence of the court, and its right to make an appropriate order based on the specific circumstances of a case. It is recommended that the word "must" be replace with "may" or "should".

In the light of the seriousness of the circumstances listed in subsection 162(5) it is recommended that a "*breach of trust*" in subsection 162(5)(c)(iv)(aa) be amended to "***wilful*** *breach of trust*".

It is unclear why subsection 162(5) refers repeatedly to "gross…" abuse or negligence. It is recommended that the word "gross" be deleted from this subsection.

It would appear that the court's discretion is unduly restricted by the wording of subsections 162(5)(d) and (e), which may have unreasonable consequences or result in an injustice. The ambit of the two subsections will include minor or technical transgressions which may not necessarily justify declaring a director as delinquent. It is recommended that the court be granted the same discretion it has in the case of subsection 162(5)(f)(ii) (i.e. "having regard to the nature of the contraventions").

It is unclear from subsection 162(7)(a)(i) whether the insolvency and liquidity tests should apply before the resolutions were considered (i.e. the current state of the company, irrespective of whatever resolution is being considered), or whether the tests would be applicable after such resolution (i.e. the impact of the resolution was to cause the tests to fail). Clarity is required.

Subsection 162(10)(c) seems to import the concept of punitive damages which is not part of South African law. This subsection unduly and without a rational basis widens the scope for damages claims in South African law as it is not based on either the sound principles of delict or contract. It is recommended that the subsection be deleted.

Similarly, subsection 162(12)(a) states that "court may not grant the order applied for unless…". This could again be challenged as interference in the court's independence, and should be amended.

2.96 **Section 163 – Relief from offensive or prejudicial conduct.**

Creditors should also be afforded the right to seek relief from oppressive or prejudicial conduct as provided for in subsection 163(1). It is recommended that the words "**or creditor**" be inserted after the words "*or a director*".

It is unclear how or why a court would want (subsection 163(2)(d)) to "create or amend a unanimous shareholder agreement". Per definition "unanimous" represents total consensus, and a consenting shareholder should not subsequently be enabled by the courts to amend such consensus or agreement. It is recommended that the words "…or to create or amend a unanimous shareholder agreement" be deleted.

2.97 **Section 164 – Dissenting shareholders appraisal rights**

It would appear that the last part of subsection 164(2)(b) commencing with "*that notice must include a statement …*" should apply to the whole of sub-section (2).

We submit that subsections 164(5)(b) and (c) could be used to unduly frustrate the legitimate and fair actions by a vast majority of shareholders. The relevant shareholder addressed in these subsections should be required to show that he or she will be unfairly prejudiced by the actions taken by the company, in order to be entitled to receive fair value for its shares. In fact, it would appear that the subsection can serve as an effective mechanism to frustrate a transaction which has been duly authorised by the requisite majorities under proper procedures. It is recommended that a court should be given a discretion whether to grant a shareholder the right of compensation or to refuse it, in the light of all relevant circumstances.

2.98 **Section 166 – 172; 182; 195**

As noted previously, the role of the new Companies Ombud in these sections is more akin to that of an appeal tribunal or other administrative body.

2.99 **Section 166 – Alternative dispute resolution**

It is inappropriate to refer to arbitration in this section. By definition, arbitration involves a ruling by the arbitrator on the dispute, and therefore should not produce a certificate stating that the process has failed. This is possible in the case of mediation or conciliation proceedings. If it is the intention of the legislator to enable the parties to agree to an arbitration mechanism, or to submit the parties to a compulsory arbitration mechanism, then this should be expressly and separately stipulated. A right of appeal should then also be dealt with

2.100 **Section 167 – Dispute resolution may result in consent order**

Subsection 167(1) refers to an instance where the Companies Ombud or the relevant entity has "resolved" a dispute. This implies that the matter was subjected to arbitration. The provisions of this section should obviously be co-ordinated with the provisions of section 166, in the light of our comments above.

Further, subsection 167(2) gives the impression that the application for a consent order may be opposed by one of the parties to the dispute because the court may refuse or alter it. Does this imply that the parties have the right to a *de novo* hearing before the court on the issue which was resolved? Depending on whether the intention of the legislator is to subject the parties to a compulsory arbitration, it is also not entirely clear whether the purpose of

section 167 is to ensure that the resolution is enforceable, or to give the parties the right of appeal or review of the process. Clarity is required.

2.101 **Section 171 – Issuance of compliance notices**

Court processes, in certain instances, literally take years. It is also unclear how effectively the other structures created in terms of this Bill will function. Under these circumstances it would not be administratively fair that a compliance notice should remain in force pending a review of the notice by the mentioned institutions or persons (subsection 171(5)). A company may be obliged to then comply with the notice in the interim and if it is successful upon referral or review therefore, it would have wrongly done so. It is therefore recommended that this subsection be amended to pend the application of any compliance notices until the completion of any review processes.

Subsection 171(5) read with subsection 172(1) also only seem to refer to a process of review. We would suggest that after a compliance notice has been issued as contemplated in subsection 171(1), the company or person against whom such notice was issued should have the right of appeal or review upon application to the institutions or persons set out in subsection 171(5)(a).

2.102 **Section 175 – Administrative fines**

It is recommended that a respondent company (i.e. not only the applicant as proposed in subsection 175(1)) should be able to bring any other relevant factors or circumstances to a court's attention in determining the appropriate administrative fine.

2.103 **Sections 176, 179 and 212**

It is recommended that these sections should explicitly protect any person's right to legal privilege. Such legally privileged information would always qualify as confidential information. However, not all confidential information is legally privileged and therefore the intention of these sections should not be undermined by the protection of legal privilege. This same principle is applied to attorneys in the Financial Intelligence Centre Act, 2001.

2.104 **Section 203 – Establishment and composition of council**

It would be advisable for a timeline to be inserted for the establishment of the Financial Reporting Standards Council, and its recommendations to the Minister for the publication of the appropriate standards. In the event that the establishment of the Council were to take an inordinate amount of time, and/or it be inadequately resourced to perform its functions, it would expose the Bill to possible abuse. It is therefore recommended that the commencement of the Bill be made subject to the establishment of the Financial Reporting Standards Council and the issuing of the regulations per subsection 204(c).

2.105 **Section 210 – Finances**

The financing proposals for the Commission, the Companies Ombud and the Panel are noted. However, it is unclear how the Financial Reporting Standards Council will be funded, as it will presumably require dedicated resources to fulfill its role.

2.106 **Section 214 – Breach of confidence**

It is recommended that the definition of "*knowingly or know*", as defined in section 1, should not find application in this section where certain actions are

criminalised. Actual knowledge should be required where criminal sanctions apply.

Further, the provisions of subsection 214(3) support the need for the recommendations in relation to subsection 171(5) above in that the compliance with or enforcement of a compliance notice should be suspended pending a decision by the relevant institutions or persons.

2.107 **Section 215 – Hindering administration of the Act**

It is recommended that actual knowledge should be required under subsection 215(2)(e) than the definition of "*knowingly*".

2.108 **Section 218 – Civil actions**

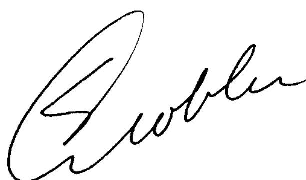
We are opposed to any interpretation that may lead to strict (faultless) liability. Damages are adequately covered in the common law. It is therefore recommended that subsection 218(2) be deleted.

2.109 **General – Chapter 9**

Include a section in Chapter 9 stating that any administrative proceedings in terms of the Bill shall comply with the provisions of the Promotion of Administration of Justice Act (PAJA), or that any decisions made or actions taken under this Bill shall be deemed to be administrative actions in terms of PAJA.

3. **Conclusion**

We thank the Portfolio Committee for this opportunity to comment on the draft Companies Bill, as well as raising our general concerns, in particular about the short time allowed for public preparation and mandating of such comments.



S. GROBLER **8 August 2008**