BALANCING MAJORITY SHAREHOLDER RIGHTS, MINORITY SHAREHOLDER RIGHTS AND CREDITORS'RIGHTS IN STATUTORY MERGERS IN TERMS OF THE COMPANIES ACT 71 OF 2008

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ABSTRACT

Companies in their various forms are crucial to South Africa's economy and its prosperity as they contribute towards wealth creation, social renewal and social welfare. In our growing world and borderless international markets, there are ongoing changes that affects a company's competitiveness and productivity both nationally and internationally. These changes may be brought by the necessity to abide by international company law standards and practices that to some extent are aiming at sustainable economic growth and profitability. The South African company law regime, introduced since 1926, has undergone a series of amendments to ensure that its national companies and stakeholders benefit from the most updated legal system to galvanise its economy. In so doing, mergers and acquisitions represent one of the most cutting-edge concepts of company law around the world that encompasses the social, economic and financial needs of companies and that have been introduced in the current national company law regime.

This research paper analyses the protections of shareholders and creditors in the statutory merger contained in the Companies Act 71 of 2008. It discusses also whether these protections are adequately balanced towards a fair consideration of majority shareholders, minority shareholders and creditors' interests — *which includes consideration of their rights too* — in implementing a statutory merger. The main findings are that some protections are not properly balanced in consideration of the aforementioned parties' interests. These include the appraisal remedy, the merger agreement and the oppression remedy — between minority and majority shareholders — and the creditors' notification coupled with the court review, the open transferability of creditors' contracts and the solvency and liquidity test — between majority shareholders and creditors — which in some aspects offers uncertainty in protecting their applicants. The approach adopted in the Canadian cases of *Black & Decker* and *Loeb*, set out in section 2 below, emphasises the importance of policy considerations which must meet the stated goals of s7 of the Companies Act 71 of 2008.

Keywords: Statutory merger, majority shareholders, minority shareholders, creditors.

TABLE OF CONTENTS

SECTION I: GENERAL INTRODUCTION

I- BACKGROUND

Prior to the enactment of the Companies Act 71 of 2008 ('Act'), a merger as a fundamental transaction *was not codified* in the Companies Act 61 of 1973 ('1973 Act') as a method of business combinations. South African companies that wanted to implement a fundamental transaction could do so only through a scheme of arrangement, a tender offer, and a sale of a business as a going concern.[1]

In alignment with international standards, the merger process was introduced in South Africa ('SA'). This was done in tandem with the goals of a new company law regime, following a review of the 1973 Act. The aim was to ensure company efficiency by reforming the merger process, facilitating the creation of business combinations, encouraging transparency with a view of protecting shareholders' rights, and providing a predictable and effective regulatory environment.[2] In so doing, it aimed 'not [to] create artificial preferences and distortions, where these are unnecessary. [But] … to balance the competing interests of economic actors [shareholders and creditors]'.[3] The review identified the fundamental rules governing the procedures for mergers and acquisitions while considering the relationship between company law and other measures for protecting the interests of shareholders and creditors.[4] It also ensured that there is integrity in the market and includes additional elements that consider the value of facilitating the restructuring of businesses in the interests of economic growth; and the interests of shareholders in retaining and safeguarding their investment against undue dilution or loss.[5]

The extent to which it fairly and simultaneously considers the rights of shareholders and creditors in the existing remedies available in the Act is the subject of this study.

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[1] Ss 228, 311–13 and 440K of the 1973 Act.
[2] The Department of Trade and Industry ('The DTI'), 'South African Company Law for the 21st Century: A Guideline for Corporate Law Reform' (2004) 3–4, available at *https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf* , accessed on 22 February 2020.
[3] The DTI op cit note 2 at 8.
[4] Ibid at 10.
[5] FHI Cassim, Maleka F. Cassim, Rehana Cassim et al *Contemporary Company Law* 2 ed (2012) 677.

II- INTRODUCTION

The statutory merger ('merger'), referred to as an 'amalgamation or merger'[6] in the Act, 'is essentially a simple, uncomplicated, and effective procedure in terms of which two or more companies may merge by agreement with the approval of the prescribed majority of their shareholders.'[7] There is no mandatory intervention of the court in this process. It is contained in s 113 of the Act under the terms 'merger or amalgamation' both of which hold the same meaning and produce the same effect — the fusion of companies.[8] A fundamental distinction between these terms is that 'a merger results in the fusion of one merging company into the other, but an amalgamation results in the fusion of all merging companies into a new company'.[9] The Canada Business Corporation Act ('CBCA') also makes no distinction between the two procedures.[10]

The purpose of this research is to analyse the protections of shareholders and creditors in the merger and to discuss whether they are biased towards minority or majority 'will' or balanced towards a fair consideration of these stakeholders' rights in its implementation. I reference United States ('US') case law because the merger provisions in the Act are inspired and drafted with reference to some principles of American company law.[11] Because of the Canadian influence in the drafting of the Act, some reference will also be made to Canadian merger law principles.[12]

As stated above, the concept is originally an American concept[13] and was introduced in SA to ensure company efficiency and to protect shareholders' rights and creditors' interests,[14] while promoting the easier facilitation of business combinations.[15] This is key to the overarching purpose of the Act to promote flexibility and enhance efficiency in our national economy[16] as provided in s 7 of the Act.

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[6] Ss 113 and 116 of the Act.
[7] MF Cassim 'The statutory merger in South Africa' (2008) 16 *Juta Business Law* 40.
[8] MF Cassim 'The Introduction of the Statutory merger in South African Corporate Law: Majority Rule Offset by the Appraisal Right (Part 1)' (2008) 20 *SA Merc LJ* 2–3.
[9] Ibid.
[10] Ss 181–189 of the Canada Business Corporation Act 1985 RS C-44 ('CBCA').
[11] Nigel Boardman 'A critical analysis of the New South African takeover laws as proposed under the Act' 2010 *Acta Juridica*, 306–7.
[12] Ezra Davis, Trevor Norwitz and David Yuill 'A microscopic analysis of the new merger and amalgamation provision in the companies Act 71 of 2008' 2010 *Acta Juridica* 338.
[13] Byron Lloyd Nicol 'The Legal Effect of Amalgamations and Mergers upon Third-party Contracts containing Anti-transfer Provisions' (2013) 25 *SA Merc LJ* 1.
[14] The DTI op cit note 2 at 12.
[15] Memorandum on the Objects of the Companies Bill, 2008, Companies Bill [B 61D-2008] para 1.2.
[16] Ibid para 9.

Due to their economic importance and vital role in the proper allocation of society's resources, mergers require intense scrutiny. If implemented, a merger has far-reaching consequences for the whole company, yet can be put into effect by only the shareholders.[17] An important consequence is that, by operation of law,[18] the merged company — the surviving company or the newly created company — holds the assets and liabilities that were held by any of the merging companies immediately before the implementation of the agreement.[19] This results in the merged company having to account for a larger pool of creditors' debts to settle, and a larger number of shares, for shareholders to allocate among themselves. These are just two concerns — *not exhaustive* — highlighting some far-reaching consequences.

The concept seems — based on its procedure and effect — to favour the 'will' of majority shareholders ('majorities') over those of minority shareholders ('minorities') and the company's creditors. However, there are protective measures for these stakeholders incorporated into the relevant sections of the Act which are discussed below; but they have loopholes — areas of ambivalence and uncertainty. The different loopholes in the protection are found in the areas of the Act that relate to the approval of the merger, the merger agreement, the valuation of shares, the creditors' notification coupled with court intervention and the solvency and liquidity test. These loopholes have the potential to put the rights of creditors and minorities at risk. Those risks, which are brought about by changes that affect the corporate structure, culture, management, the juristic personality of the company,[20] and the original investment expectations, may be prejudicial to these stakeholders.[21]

Accordingly, other legal remedies such as the appraisal remedy for dissenting shareholders ('dissenters') and the court intervention under s 115 of the Act for dissenting creditors ('creditors') exist for those who view the merger as detrimental to their interests. These will affect the proposed merger and may override the decision of their majority to approve it.

III- RESEARCH PROBLEM

[17] S 115 of the Act.
[18] S 116(7) of the Act.
[19] Ibid.
[20] In the event the merging companies after the merger creates a new company.
[21] Milton Seligson SC 'Dissenting Minority Shareholders' Appraisal Rights: Reappraising the appraisal remedy in section 164 of the companies Act 71 of 2008' (2016) 7 *Business Tax & Company Law Quarterly* 3–4.

After identifying potential harm to majorities, minorities and creditors, I consider if the aims of the DTI document issued in 2004 and embodied in s7 of the Act were fully met. These objectives stated that the review of company law will consider 'measures for protection of the interests of shareholders [and] creditors'.[22] The purpose of this research is to identify the measures for the protection of majorities, minorities and creditors, and to critically assess their fairness in terms of the level of exposure of each stakeholder to the risks inherent in the merger process.

To do this, I address the following questions:

1. What are the measures that protect minorities and creditors who may be prejudiced by the majorities?
2. What are the limits of the protections afforded to minorities and creditors?
3. Do those measures provide a fair balance between the rights and interests of the majorities, the minorities and the creditors?

[22] The DTI op cit note 2 at 12.

SECTION II: CRITICAL ASSESSMENT OF THE MERGER PROVISIONS

I- CONTEXT AND POLICY CONSIDERATIONS

The concept of merger does not hold the same meaning in SA as in the US.[23] In the US, it is a long-standing practice of business combinations that had three distinct movements from 1898 to 1940.[24] It referred to the disappearance or appearance of a company pursuant to an agreement or consolidation as the case may be.[25] In SA, before the Act, the term 'merger' or 'amalgamation' referred to transactions whereby a company acquires control of the assets of the other 'merging' company either through business combinations — a scheme of arrangement, a tender offer and a sale of a business as a going concern.[26] The 1973 Act had not specifically provided for merger although mentioning 'amalgamation' in its provision for business combination as '…the compromise or arrangement [that] has been proposed for the purpose of … the amalgamation of two or more companies…'.[27]

Merger in the Act was designed to transfer the whole of a business and not part of it and to lead to the automatic dissolving of the merging company by operation of law.[28] The old procedures might have the same broad objective — business combination — but did not have the same ambit of a merger. The Supreme Court of Canada in *R v Black & Decker Manufacturing Co. Limited*[29] established the principle that an amalgamated company is a continuation of the amalgamating companies, and that the end result of an amalgamation is 'to coalesce to create a homogeneous whole'.[30] The court in *Loeb Inc v Cooper*[31] determined that the property and the rights of each amalgamating companies continue to be the property and rights of the amalgamated company. Both cases stressed that upon an amalgamation, no 'new' company is created and no 'old' company is extinguished. The effect is that of blending and continuance as one and the self-same company that serve to guarantee that an amalgamation does not absolve any merging company from its liability towards other stakeholders, i.e. creditors.

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[23] Ibid at 340.
[24] Carl Eis 'The 1919-1930 Merger movement in American Industry' (1969) 12 *J.L & Econ.* 267.
[25] § 251(c) Delaware General Corporation Law Title 8 Chapter 1 ('DGCL'). See also Carl Eis op cit note 24 at 270.
[26] Ss 228, 311–13 and 440K of the Act 1973. See also HS Cilliers, ML Benade, JJ Henning, et al *Corporate Law* 3 ed (2000) 460–461.
[27] S 313 of the 1973 Act. See also Ezra Davis et al op cit note 12 at 340.
[28] Ibid at 343.
[29] (1974), [1975] 1 SCR 411, 1 NR 299.
[30] Ibid para 421.
[31] (1991), 5 OR (3d) 259, 3 BLR (2d) 8 (CJ).

Based on the influence of the common law in our judiciary system, the approach adopted in *Black & Decker* and *Loeb* will weight considerably in balancing the interests of various parties at stake during implementation of a merger in SA.

In the Act, s 113 sets out the process of a merger. This includes the requirements of the constituents' parties (only companies and a minimum of two), the merger agreement, the solvency and liquidity test and a notice of a shareholders meeting. Section 115 deals with the required approval of shareholders necessary for the passing of the merger during a special resolution, and; s 116 lays out the creditors' implication in the approval of the merger. From the provisions of ss 113 and 115, it is clear that the Act is shareholder-centric — placing a strong emphasis on the protections of shareholders' interests and the need of the board of merging companies to obtain their approval prior to implementing a merger.

II- UNALTERABLE PROVISION BENEFITING THE MAJORITIES

One of the laudable changes brought about by the Act is the concept of unalterable provision as defined in s 1 of the Act.[32] It introduces 'rigidity' in structuring a company instruments necessary to cater for the investment objectives of its pool of investors, and in the control and economic schemes of that company. In *Farren v Sun Service SA Phot Trip Management (Pty) Ltd ('Farren')*[33] Cleaver J stated that a transaction that has the effect of resulting in a disposal of all or a greater part of the company must strictly respect the internal requirements laid down by statute and not by a company's document.[34] Although merger was not codified in the 1973 Act, the same procedural 'rigidity' applies for the procedure of merger in the Act. Cleaver J's statement was made with an emphasis on the necessity to protect shareholders interests' in the transaction aforementioned. While having merits at the time, with merger, it is important to adopt a balanced approach especially because it is an unalterable transaction, and that minorities who do not weight much in the writing of the Memorandum of Incorporation (MoI) and the shareholder agreement, and creditors who do not participate in the writing of these documents, cannot protect their interests based on these company's document.[35]

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[32] Michael M. Katz 'Governance under the Companies Act 71 of 2008: Flexibility is the keyword' 2010 *Acta Juridica* 249.
[33] 2004 (2) SA 146 (C).
[34] Richard Jooste 'Observations on the Impact of the 2008 Companies Act on the doctrine of constructive notice and the Turquand rule' 2013 *SALJ* 466.
[35] MF Cassim (part 1) op cit note 8 at 11.

SECTION III: THE PROTECTION AFFORDED TO SHAREHOLDERS

One of the founding principles of South African company law is the majority rule that confers the power to majority of the votes to decide the company affairs at the expense of the minorities.[36] For instance, it is present in the requirements of the shareholder approval and quorum where the passing of a merger heavily relies on the approval of the dominant majority. This might be detrimental for minorities during the merger procedure in terms of voting rights and the unfair treatment they might be exposed to in case the transaction may not be implemented to 'truly' serve the company's interest as a whole.

Based on the following, the merger provisions in the Act chose to provide more protection to the minorities than its counterpart in US jurisdiction which is considered more board-centric.[37] The legislator chose to retain a shareholder-centric approach as a policy preference. In so doing, they are afforded a set of protections with different purposes.

In this part, I look at each of the protections available to shareholders with an emphasis on minorities.

I- DIRECT PROTECTIONS

'Direct' protections relate to remedies in the Act *not limited to minorities* (except only for the appraisal remedy) *although typically it is minorities who invoke them.* These include the oppression remedy, the court review and the board's fiduciary duties. I will critically discuss their balancing effects compared to the majority's interests.

(a) The appraisal remedy ('appraisal')

The appraisal is the prime protective defence for dissenters[38] provided in s 164 of the Act. It allows them, in the event of a merger being undertaken by a company with which they disagree, to require the company to acquire their shares at fair value determined by the court.[39] Its

[36] HS Cilliers, ML Benade et al op cit note 26 at 296. See also Natasha Bouwman 'Majority rule and minority protections' 2010 *Without Prejudice* 12.
[37] Ezra Davis et al op cit note 12 at 339.
[38] HGJ Beukes 'An introduction to the Appraisal Remedy in the Companies Act 2008: Standing and the appraisal procedure' (2010) 22 *SA Merc LJ* 177.
[39] S 164(14)*(a)* of the Act. See also Allen & Kraakman *Commentaries and Cases on the Law of Business Organisations* 5 ed (2003) 452; Neil Finkelstein 'Expropriation of Minority Interests and the Appraisal Remedy' (1985) 27 *Business Law Reports* 234; Stephen M Bainbridge *Corporation Law and Economics* (2002) 632.

particularity dwells in the granting of a means of exiting the business of the merging company and challenging the fairness of the consideration that they receive for their shares.[40]

(i) The balancing effect

First, one of the main powers of the appraisal lies in its economic aspect in protecting the investment of minorities in a company in case of disapproval of a merger. The Act states that in case of a relationship breakdown due to disapproval of a merger between shareholders, the court must make an order requiring dissenters to either withdraw their respective demands or tender their shares to the company in return for the judiciary determined fair value of their shares.[41] However, there is no clear meaning to what 'dissenting shareholders to either withdraw their respective demands (and be reinstate to their full rights as a shareholder)'[42] entails which lead to uncertainty for this specific outcome. In a merger, dissenters have their 'full rights' contemplated in the agreement to the extent that their shareholdings allow them to be made an offer by the acquiring company. In contrast, post-merger, 'full rights as a shareholder' refer to dissenters remaining as shareholder in the merged company. Which interpretation is to be accepted?

There is also uncertainty behind the exact meaning of 'varying a corporation obligation' between academics and legal practitioners.[43] This affects the balancing of rights between majorities and minorities. Reinstating dissenters' rights in respect of the tendered shares does not appear to uphold the cumulative conditions of s 164(17)*(b)* that suggest the court order to be made justly and equitably as well as the payment to be made timeously. Considering that dissenters and the company would have agreed on a fair value of the shares means that both parties have no interests in having dissenters remaining as shareholders but that the critical issue lies in having adequate payment terms that will benefit majorities and minorities.

Secondly, standing to bring the appraisal can be interpreted in a more limited or extended way. Depending on which interpretation is used, the balancing effect of the remedy may be diluted. On the limited standing, if the company is entitled to 'regulate' the remedy and restrict the standing of 'newly' registered or beneficial shareholders and existing shareholders who would

[40] Ezra Davis et al op cit note 12 at 352.
[41] s 164(15)*(c)(v)* of the Act.
[42] s 164(15)*(v)* of the Act.
[43] See the dissenting views between HGJ Beukes op cit note 38 (academic) and Adam Pike (legal practitioner) 'An Alternative view of the Appraisal remedy' (2014) 26 *SA Merc LJ*.

like to 'enrich' themselves through appraisal,[44] then it is because appraisal is afforded to bona fide shareholder not to opportunistic one.[45] While I understand such rationale, I disagree because this could undermine the balancing interests of majorities and minorities. First, it is a statutory right afforded to dissenters through the Act, not by the company. Secondly, it is a protection against majority rule that in most scenarios control or exercise their power over the board that runs the company. It is highly controversial to allow the one against which the remedy was created to have the power under certain circumstances to restrict its use. Also, the argument of 'bona fide' shareholder remains a doctrinal issue as it is highly subjective to determine with certainty whether dissenters[46] are triggering the remedy in good faith or not. In Canada, in *Silber v. Pointer Exploration Corp.,*[47] the court suggested that whoever becomes shareholder after the company has given notice of a meeting at which a resolution will be considered to take a triggering action, was permissible to exercise his appraisal.[48]

Regarding the extending standing, s 157(1)*(b)* of the Act allows a person acting on behalf of interested third party contemplated in para *(a), (c)* and *(d)* to use the remedy. The extension goes to 'beneficial shareholders' referred to in s 56 of the Act, and that they should have standing too on the basis of the application of analogous Canadian case law.[49] I believe that it promotes a balancing approach between majorities and minorities. It guarantees the use of the remedy even in the context where dissenters could not exercise themselves their rights.[50]

Thirdly, partial dissent does not trigger appraisal[51] and remains an unsettled matter in the Act[52] unlike in the CBCA.[53] The CBCA envisages a pool of shares with various beneficial shareholders where a merger might adversely affect one of the beneficial shareholders not a class of shares per se. But ss 164(5) and (9) of the Act do not. They raise, however, a question about whether partial dissent is permissible when there is a pool of shares with one holder, and

[44] HGJ Beukes op cit note 38 at 179.
[45] Ibid.
[46] Irrespective of the time of his registration.
[47] (1998) 42 BLR (2d) 149 (Alta QB), the Alberta Court of Queen's Bench stated that if the company wanted to control the right of holder of shares to make use or not of their appraisal right, it could have expressly said so in the information circular that only holders of shares registered at the date of that circular were allowed to exercise their appraisal remedy.
[48] Ibid at 157. See also Christopher C Nicholls *Corporate law* (2005) at 457–58.
[49] Adam Pike op cit note 43 at 679.
[50] Ibid at 680.
[51] S 164(5) of the Act. See also HGJ Beukes op cit note 38 at 184.
[52] S 164 (9) of the Act. See also HGJ beukes op cit note 38 at 184.
[53] S 190(4) of the CBCA.

that holder of shares might find himself in a position where one of his class of shares might be prejudiced by the transaction.

Accordingly, ss 164(5) and (9) of the Act have advantages and disadvantages for two reasons. First, partial dissent could be translated into an overemphasis on minorities rights and lead to minority 'dictatorship' within the merging company. Until a merger is 'perfect' to the extent that it favours unanimously all class of shares, any holder of any class of shares prejudiced by its implementation would be entitled to the appraisal. Such interpretation could hamper the flexibility sought by the Act.[54]

Furthermore, the rationale of different exposure as per the class of shares is a critical matter and cannot be overlooked by our courts. It is reasonable to envisage a scenario where dissenters might face a deadlock between approving or dissenting a merger based on its effect on one of their classes of shares. Whether the disadvantaged class of shares represents a consistent percentage of dissenters' portfolio could form part of the assessment in deciding whether to allow them partial dissent and to demand that the merging company purchase their shares for this specific class of shares. In any case, the legislature should consider this matter as it serves in balancing the rights and interests of majorities and minorities during implementation of a merger.[55]

Finally, the appraisal with the court's involvement serves to reinforce the fiduciary duties of the board towards its shareholders as it reduces the overprotection that could have resulted in the event where the board was the only party entitled to determine the fair value of a share. 'Any attempt to circumvent reliance on it will be found inconsistent with the Act and void or may even fall foul of the anti-avoidance provisions.'[56]

(b) The oppression remedy ('relief')

The protection is provided under s 163 of the Act and allows a shareholder to apply to court for relief if he can demonstrate that any conduct of the company or its directors or officers has been oppressive or unfairly prejudicial to him or unfairly disregard his interests. It has several aspects.

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[54] Michael M. Katz op cit note 32 at 248–53.
[55] FHI Cassim et al op cit note 5 at 807–808.
[56] S. Dwyer and L. Ngwenya 'Using the appraisal remedy and finding fair value' 2013 *Without Prejudice* at 8.

(i) The balancing effect

The relief is the statutory answer to the limited scope of application of the appraisal.[57] It properly balances the right of majorities and minorities for three reasons. First it is available to any shareholder with no requirement of having previously voted against the merger resolution. It is wider than the appraisal. It includes dissenters who could not vote because they did/could not attend the shareholder meeting and would like to oppose the passing of the merger resolution.[58] It balances the majority's rule by imposing on majorities a duty to act fairly on behalf of all shareholders.[59] Section 163 entitles minorities to bypass the traditional overemphasis in *Foss v. Harbottle*, which precluded derivative actions on behalf of the company where an act was ratifiable by giving them a direct action for relief without having to sue on behalf of the company.[60]

Secondly, it appears to allow for more grounds[61] than the court intervention under s 115, which allows the court to set aside a merger resolution only under two specific grounds.

Thirdly, it provides the court with a wider set of remedial powers and applicant with a broader choice of outcome.[62]

However, as any court remedy, dissenters might be disincentivised by the costs and time-consuming procedure and will have to solely bear the costs of proceedings unlike the s 115 procedure of the Act. In addition, its balancing effect might be challenged with the uncertainty in drawing a line between what is 'oppressive', or 'unfair'.[63]

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[57] Nkululeko Masondo *The protections of shareholders and creditors in the context of takeovers and reorganisations under the Companies Act 71 of 2008* (LLM dissertation, University of Pretoria, 2018) 11–12.
[58] Ibid.
[59] Philip Anisman 'Majority-Minority Relations in Canadian Corporation Law: An Overview' (1998) 13 *Canada-United States Law Journal* 89–90. See also *Clemens v. Clemens Bros* (1976), [1976] 2 All E.R. 268 (Ch.). The court decision disallowed amendments to a company's articles of association which would have deprived a minority shareholder of her negative control and entitled the majority to pass a special resolution alone.
[60] Philip Anisman op cit note 59 at 90.
[61] S 163(1) of the Act.
[62] S 163 (2) of the Act.
[63] Philip Anisman op cit note 59 at 87.

(c) The court review

This refers to the reviewing/setting aside of the transaction.[64] If there are 15 per cent or more dissenting votes among the voting rights, dissenters may require the company to seek court approval and the merger will be pending until court approval.[65] The company decides whether to apply for court approval and bear the cost of the application; if not, to treat the resolution as a nullity. Regardless of the 15 per cent threshold being reached or not, dissenters may use the remedy provided they satisfied the requirements of the Act.[66]

(i) The balancing effect

First, the grounds on which a court decides to review/set aside a merger resolution are very limited. It requires *manifest unfairness* to any class of shareholders and procedural irregularities evidenced by a *materially tainted* transaction.[67] This approach was also followed in the Delaware court generally applying the business judgment rule when reviewing challenges to merger and similar transactions.[68]

Secondly, the financial cost attached to a court application represents a considerable dilution of the protection available to dissenters.[69] When the latter holds an 'insignificant' percentage of shares with voting rights, and that the cost of application is more important than remaining as shareholders in the merging company, there might be a risk of disincentivising dissenters to use this remedy. This is likely to happen when the 15 per cent threshold for dissenting votes is not met since the Act does not make it mandatory for the company to bear the cost of application.[70] Why would the Act choose a 15 per cent not a 5 per cent threshold for dissenting votes to allocate the cost of application to a company? This could have widened the pool of minorities that could have relied on it should their interests being at risk and their *financial capacities* being the *main hurdle* in their use of the remedy.

Thirdly, a court application is not available to those who did not vote against the transaction but who nevertheless may be materially prejudiced by it. Such exclusion poses a 'procedural

[64] MF Cassim (part 1) op cit note 8 at 13.
[65] S 115(3) of the Act.
[66] S 115(6) of the Act.
[67] Ezra Davis et al op cit note 12 at 359.
[68] *Smith v Van Gorkom* 488 A2d 858 (Del 1985) 1–5, available at https://www.law.upenn.edu/live/files/6512-a-hreflivefiles6512-smith-v-van-gorkom-488-a2d-858, accessed 28 January 2020.
[69] Ezra Davis et al op cit note 12 at 363–64.
[70] S 115(5)*(a)* of the Act.

fairness' threat on the side of the company, although shareholders unable to personally vote during the resolution could have done so via their representatives duly equipped with proxy. Dissenters who could not vote against the merger should be afforded the right to dispute it, save that they can provide the court with reasonable grounds justifying their absence, and that the prejudiced is real, direct, immediate and linked to the merger.

(d) The board's fiduciary duties

In terms of s 76(2) of the Act, directors owe fiduciary duties to their company, and they have a duty to act in the best interest of the company. Fiduciary duties, specifically the duty to act in good faith for a proper purpose in the best interest of the company and the duty to exercise an unfettered discretion, require the directors of the merging company to consider objectively whether the merger is in the best interest of the company as a whole.[71]

(i) The balancing effect

It is important to assess the balancing aspect of this remedy for two reasons. First, because in a merger, shareholders do not negotiate the terms of the agreement.[72] Secondly, because a zealous acquirer could offer excessively generous side-payments to the board to obtain their cooperation and cloud their judgment.[73] Therefore, it is crucial that those entrusted to protect the interest of the company as a whole do so honestly while making a properly informed decision.

The Delaware Court of Chancery was of that view and stated in *Sealy Mattress Co of NJ, Inc v Sealy Inc.*[74] in relation to directors' duty of care and skill that a merger that has not been the subject of a properly informed director judgment may not be submitted to shareholders. In *Smith*, the court decided that a proper exercise of directors' duty of care and skill in the context of a merger would arguably require a recommendation from knowledgeable outsiders experts be made to shareholders on the merits of the agreement.[75] Unfortunately, the Act does not make such express provision unlike the American Revised Model Business Corporation Act 1984.[76]

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[71] S 76(3) of the Act.
[72] MF Cassim (part 1) op cit note 8 at 16.
[73] Ibid at 15.
[74] 532 A 2d 1324 (Del Ch, 1987).
[75] *Smith* supra note 68 at 1–5.
[76] S 11.04*(b)* of the American Revised Model Business Corporation Act 1984 specifically requires the directors to transmit to the shareholders a recommendation regarding their approval of the merger.

However, the Act authorises shareholders to also require additional information on the material interest of the directors in the merger.[77] The duty of disclosure contained in such a requirement may serve to counterbalance the lack of statutory requirement for having an independent expert's report coupled with the directors' recommendation on the merger.

II- INDIRECT PROTECTIONS

These are remedies that are *in my view* not specifically designed for minorities but for shareholders as a whole and represent safeguards for their rights balanced with those of the board. These include the merger agreement, the shareholder approval, and the judiciary valuation of shares. I will discuss their rationale and critically assess their balancing effects.

(a) The merger agreement ('agreement')

The agreement is a statutory prerequisite that must be entered between merging companies in terms of s 113(2) of the Act. It sets out the terms of and means of effecting the merger i.e. the MoI of the merged company; the manner of payment of any consideration.[78] Traditionally, all liabilities of a merging company would vest into the merged company. However, the Act allows the agreement to set specific terms dealing with the matter[79] subject to the requirements of s 113(1).

(i) The balancing effect

Formalism is a pre-requisite in implementing a merger as evidenced by the mandatory requirements of s 113(2) of the Act. Merging parties must enter into an agreement that clearly specifies every aspect of the transaction. However, such protection seems limited since companies have leeway in deciding the structure of the merger according to their requirements[80] and in deciding the consideration of payment. This could critically dilute the efficiency of the agreement in protecting the right of minorities when the sole purpose of the transaction is towards the interest of the majorities.

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[77] S 75 of the Act.
[78] S 113(2)–(5) of the Act.
[79] S 116 (7)*(b)* of the Act.
[80] Ezra Davis et al op cit note 12 at 344.

First, there are some merger structure that bypass the need of approval. For instance, an acquiring entity (A) could acquire the target (T) through a reverse triangular merger[81] in which (A) creates a merger subsidiary (S) that merges into (T), with (T) surviving the merger as a wholly owned subsidiary of (A), and (T)'s shareholders receiving shares in (A). Shareholders of (A) can clearly assess the profitability of (T) and would not need the approval of shareholders (S) in deciding to acquire (T). This is problematic for minorities in (S) that could be prejudiced in case the transfer of liabilities appears to be more important than before implementation of the merger.

Secondly, traditionally, in a merger, consideration of payments between shareholders of the merging companies would be to receive shares in the merged company.[82] The Act implicitly authorises a cash consideration, gratuitous considerations, the possibility for shareholders of the merging companies to receive shares in a company other than the merged company, and any other consideration of payment that a company may think of. This is very problematic considering that it might serve to 'freeze-out' minorities and operate as a mechanism of expropriation[83] instead of a mere means of payment. For instance, when an acquirer has obtained more than 90 per cent of the shares, it could compel minorities to exchange their shares for cash. Having an expressed limited cash payment provision in the Act could reduce the risk of minorities being forced from disinvesting from the merging company. Majorities will still be entitled to offer cash payments for minorities' shares while the latter would have the right to decide whether to tender their shares for full cash or for other considerations they deem fit.

(b) The shareholder approval ('approval')

The approval mechanism which provides that a merger must be approved 'by a special resolution', is contained in s 115 of the Act. It is applicable only after the board of the merging company has applied the solvency and liquidity test and reasonably believes that the merged company will satisfy it upon implementation of the merger. It is required for shareholders of all merging companies.

[81] A merger where an acquiring company creates a subsidiary for the sake of merging it with the target company, resulting to the surviving of the target company and the dissolution of the subsidiary.
[82] Ezra Davis et al op cit note 12 at 344.
[83] Ibid at 345.

(i) The balancing effect

The approval is not mandatory and may lead to a scenario where it is bypassed by the board. First, some jurisdictions do not require the approval of the acquirer's shareholder if the acquirer is significantly larger than the target company.[84] In addition, the structure of the merger contemplated by the acquiring company may help avoiding the approval. For instance, in a reverse triangular merger, the shareholders of the acquiring company will not have to approve the transaction since their company is not a party to the merger. Such a scenario does not provide the intended protection sought by the legislator to shareholders, *nor to minorities who cannot afford the company to bypass their approval in passing the transaction if the motives are not for the interest of the company as a whole.*

Secondly, the ramification of s 115(4) of the Act on the shareholder voting requirements, especially in the context of a triangular merger[85] undermines also minorities' rights and the statutory protection afforded to them in situations where the acquirer stands on both sides of the transaction.[86] Confusion arises given the various possibilities in which a merger can be implemented, thus influencing the position of some shareholders who could have appeared as related to an acquiring party or to a person acting in concert.

Lastly, the approval is made if a quorum of shareholders entitled to exercise at least 25 per cent of the voting rights exercisable in respect of the merger are represented.[87] The quorum in the Act is specific to a category of shareholders and the nature of the transaction unlike in Canadian legislation under which each share carries a right to vote regardless of it being a non-voting share.[88] Accordingly, the approval requirements mean that approval is made by the dominant majority and not by the numerical majority. This does not adequately provide a fair protection to dissenters when all that is needed is the approval of the dominant majority. It is significant that the quorum and the prescribed approval *relate to the number of shares* and *not to the number of shareholders*.[89] This is very critical when the interest of the dominant majority does

[84] R. Kraakman, H. Hansmann, G. Hertig et al *The Anatomy of Corporate Law – A comparative and Functional Approach* (2004) 135.
[85] It involves three companies. On the target side of the transaction is the target company, while on the acquiring side are the holding company which is the would-be acquirer, together with its newly-formed, wholly-subsidiary.
[86] Marko Kershoff 'The legitimacy of the triangular merger structures: the incompatibility of sections 113(2) and 115(4) of the Companies Act 71 of 2008' 2015 *SA Mercantile Law Journal* 329–35.
[87] S 115(2)*(a)* of the Act.
[88] S 183(3) of the CBCA. See also MF Cassim (part 1) op cit note 8 at 9.
[89] MF Cassim (part 1) op cit note 8 at 9.

not align with those of the company. Another important point is the relatively low 25 per cent of voting rights needed in terms of participating at the meeting. This is not substantively representative of the decision of shareholders, at least not the majority nor half of them. For instance, in the US, most state laws set their quorum at 50 per cent of the outstanding shares; in Germany, 75 per cent of voting shareholders are required.[90]

Moreover, there seems to be an exclusion of other shareholders such as the holders of preference shares, shareholders with dual interest as in both the acquiring and the target company.[91] Authorising separate class votes increases the protection of shareholders of that class from abuse of power from the dominant majority. Conversely, in the US, shareholders having conflicting interests are authorised to vote but subject mergers involving controlling shareholders to heightened judicial scrutiny to make sure that their votes are fair to the minority.[92] Canadian legislation[93] also makes provision for class voting when the agreement contains provisions that affect the rights of other classes of shares.[94]

(c) The judicial valuation of shares

Sections 164(15)*(a)* and *(c)(ii)* of the Act require a court to determine a fair value in respect of the shares of dissenters who have not accepted an offer from the company. Section 163 of the Act also, requires a court to make a wide range of orders, including a buy-out of dissenters when necessary.[95] However, as simple as these requirements appear, valuation of shares remains a daunting task for the judiciary. As stated by Brandeis J 'value is a word of many meanings'.[96] In *Pietermaritzburg Corporation v. South African Breweries Ltd.*,[97] the court held that the proper standard of value was the market value and that 'the value of an article is as general rule what it will fetch'.[98]

This was confirmed in *IRC v. Buchanan*[99] when the court held that a value to be ascertained by reference to an offer realisable in an open market meant an intention to include every possible

[90] R. Kraakman et al op cit note 84 at 134.
[91] Ezra Davis et al op cit note 12 at 347.
[92] Ibid at 358.
[93] S 183(4) of the CBCA.
[94] MF Cassim (part 1) op cit note 8 at 12.
[95] S 163(2)*(g)* of the Act. See also Yaniv Kleitman 'Judicial valuation of shares' 2012 *Without Prejudice* 22.
[96] BC Berelowitz 'Legal Aspects of the valuation of shares' 1979 *De Rebus* 199. See also *Southwestern Telephone Bell Co. v. Public Service Commission* 262 US 276 at 310 (1923).
[97] 1911 AD 501.
[98] BC Berelowitz op cit note 96 at 199.
[99] [1914] 3 KB 466 CA.

purchaser,[100] and whether one specific purchaser was willing to pay more would influence the price but should not influence the value fixed at the price which that specific buyer would pay.

The valuation process, although including the considerations aforementioned,[101] provides a market value approach (not a price value approach) related to valuation of majority and minority shareholdings in an open market. Despite such a specific approach as stated in the *Pietermaritzburg* case, only approximate results can be obtained through the valuation process.[102]

In a more recent South African (unreported) case *Hickman v Oban Infrastructure (Pty) Ltd*,[103] the court did not apply any of the approaches aforementioned, but ruled in favour of an expert doing the valuation. This shows implicitly how valuation of shares remains difficult for the judiciary and highly exposes shareholders' interests.

(i) The balancing effect

The term 'fair value' in itself is elusive and the test for valuation of shares is far from leading to certainty.[104] As supported by James J, 'the application of valuation principles is not a matter of pure mathematics, and there is room for wide differences of opinion as to the relative weight to be given to each of the several factors in the circumstances of any particular case'.[105] Although it does not hold any certainty, it may be seen as a 'shield' protecting shareholders from an arbitrary estimation of their shares from the acquiring party, thus leading to an unbalanced protection. In this scenario, at least the arbitrariness does not come from any interested parties but comes from a disinterested party — the court. Depending on the court's findings and the market value, the valuation of shares could be lesser or higher than the corporate offer. A court valuation equally exposes majorities and minorities' interests.

[100] The principle that a market encompasses all possible buyer in general was approved in *Holt v. IRC* [1953] 2 All ER at 1501.
[101] For an in-depth analysis on the legal aspect of valuation, see also Alwyn de Koker *The legal aspects of the valuation of shares* (LLM research project University of the Witwatersrand, 1984) 1–139.
[102] BC Berelowitz op cit note 96 at 201. See also Alwyn de Koker op cit note 101 at 71–75.
[103] (NDP) unreported case no. 2008/18332 (22 July 2009).
[104] S, Dwyer and L. Ngwenya op cit note 56 at 9.
[105] *Estate Duty* Case No.1 (1958) 23 SATC 362 (N) at 366. See also Berelowitz op cit note 96 at 201.

SECTION IV: THE PROTECTION AFFORDED TO CREDITORS

Since minorities are not exclusive in their exposure to abuse by act of the company or the majorities throughout implementation of a merger,[106] this section discusses the protection afforded to creditors. Whether it refers to financial creditors, or to all contractual counterparties or even to those who may not have formal contracts[107] with the merging companies, there seems to be no clarification for the meaning of 'creditors' within the ambit of the Act.[108]

Upon implementation of the merger or post-merger, the creditors of each of the merging companies may also have their interests prejudiced. For instance, they could be competing more with one another since their preference claim may vary now according to the nature of their contract with the merging companies, the proportion of the amount in relation to the value of the merging company assets and the merged company.[109] The mechanisms provided for their protection are the application of the creditors' notification coupled with the fifteen business days to request a court review of the transaction,[110] the open transferability of creditors' contracts,[111] and the solvency and liquidity test.[112]

In this section, I look at the rationale of each remedy and will critically assess its balancing power in relation to the power of the majorities.

I- THE CREDITORS' NOTIFICATION AND COURT APPLICATION

Before implementation of the merger, written notice must be given to all known creditors of the merging companies,[113] and they have fifteen business days to request a court review of the merger.[114] The requirement of s 116(1)*(a)* is inclusive as it does not differentiate the type of creditors nor the nature of their claims.

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[106] Deborah A. DeMott 'Oppressed but not betrayed: A comparative assessment of Canadian remedies for minority shareholders and other corporate constituents' (1993) 56 *Law and Contemporary Problems* 212.
[107] Such as employees and delict victims, or contingent creditors, who regardless of their claim not yet being claimable, may be potentially materially prejudiced by the merger.
[108] Ezra Davis et al op cit note 12 at 364.
[109] Paul L Davies *Gower & Davies' Principles of Modern Company Law* 7 ed (2003) at 799.
[110] S 116(1)*(a)(b)* of the Act.
[111] S 116(7) of the Act.
[112] S 113(4)*(a)* of the Act.
[113] S 116(1)*(a)* of the Act.
[114] S 116(1)*(b)* of the Act.

The fundamental power of the notification lies in the judiciary – a remedy available to creditors' in the case of dissent. However, the protection is not absolute as it is submitted to requirements qua creditors and qua claims. The court may review the merger if it is satisfied that a creditor has no ulterior motive, is acting in good faith and that he would be materially prejudiced by the implementation of the merger, and; there are no other remedies available to protect his interests.[115] Therefore, there remains substantial room for interpretation and the exercise of the court's discretionary power into granting or not granting a creditor's application. The criteria used by the court to determine 'good faith' and 'materially prejudiced' are not certain and as seen in the literature, the doctrine of good faith is far from being an agreed and uniform matter.[116]

I believe that the balancing 'power' of this protection is in the analysis of the creditors' claims being done through the assessment of the requirements qua creditors and qua claim. The remedy albeit available, is not effective until the requirements discussed above are proven. This allows for a proper balancing of the interests at stake.

II- THE OPEN TRANSFERABILITY OF CREDITORS' CONTRACT

Upon implementation of the merger, all liabilities of the merging companies would vest upon the merged company(ies) regardless of the creditors' intention.[117] In this manner, creditors' claims are not extinguished.[118] This rule derives from the free transferability of property[119] and was confirmed in *Trust Bank of South Africa v Standard Bank of South Africa.*[120]

However, this is not absolute as s 116(7) balances it with the provision of the agreement or any other agreement existing between the merging companies and creditors. Also, s 116(7) deals

[115] Ezra Davis et al op cit note 12 at 364.
[116] Jacques Du Plessis 'Giving practical effect to good faith in the law of contract' (2018) 29 *Stellenbosch Law Review* 379–385. See also, MF Cassim 'The statutory derivative action under the Companies Act of 2008: The role of good faith' ('The role of good faith') (2013) 130 *SALJ* 507–526, although good faith was analysed in light of the requirements of s165 of the Act, the background helped me understand the controversial nature of the doctrine and the different court's approaches in recognising it or not; Andrea Opperman 'Good faith: a bona fide get-out-of-jail-free-card or a failed breakout attempt?' 2017 *Without Prejudice* 11–12;
[117] MF Cassim (part 1) op cit note 8 at 5.
[118] Ibid at 14.
[119] Byron Lloyd Nicol op cit note 13 at 52.
[120] 1968 (3) SA 166 (A) 189D.

with transfer of 'property' and 'obligations' but not transfer of contracts per se between the merging companies and creditors.[121]

(a) The balancing effect

Based on the existing contracts between the merging companies and a creditor, the latter's interests may be affected when the vesting of liabilities of the merging companies upon the merged company creates a change of debtor, and that debtor's creditworthiness is seriously questionable. This is applicable under circumstances in which creditors did not include a clear pactum de non cedendo ('pactum') in their contract with the merging companies dealing with the scenario aforementioned. An unclear pactum could raise serious concerns about the balancing of creditors' interests with those of the majorities.

In SA, the validity and effect of a pactum[122] depends on the dual nature of personal rights, and the distinction between a pactum in relation to a right already in existence (first type) and a right created for the first time (second type). It also involves consideration of the principles of freedom of contract and *pacta sunt servanda* ('pacta'). In *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd*,[123] the current position in SA regarding pacta is that a debtor should have an interest in restricting the transfer of rights in relation to the first type of pactum, whereas the second type of pactum merely prohibits a creditor from freely transferring his property as the right is non-transferable ab initio.[124] The 'rule of prejudice' in this court assessment is given a broader sense as the transfer of the right should not expose the debtor's position to more burden. Sometimes it alludes to a procedural prejudice, i.e. multiplicity of actions or increased costs,[125] or is afforded an open definition.[126] However, this needs clarity.[127]

The second type of pactum (freedom of contract) takes pre-eminence over pacta because the nature of the right is such that it is not transferable.[128] In *Nokes v Doncaster Amalgamated*

[121] Byron Lloyd Nicol op cit note 13 at 30.
[122] An agreement prohibiting cession. It may be an absolute prohibition on the transfer of a personal right or a qualified restriction on its free transferability, which requires the consent of the debtor. See also Susan Scott *The Law of Cession* 2 ed (1991) at 2.
[123] 2008 (4) SA 510 (C) 514F—515C.
[124] Byron Lloyd Nicol op cit note 13 at 54.
[125] *Van der Merwe v Nedcor Bank Bpk* 2003 (1) SA 169 (SCA).
[126] *Corinth Properties (Pty) Ltd v Firstrand Bank Ltd* 2002 (6) SA 540 (W).
[127] S W Van der Merwe et al *Contract: General Principles* 4 ed (2012) at 411.
[128] Byron Lloyd Nicol op cit note 13 at 56.

Collieries Ltd,[129] the court have laid down that purely personal contracts cannot be transferred because their very nature imposes the performance of an obligation upon a specific party or person only. In this case, the requirement that the debtor must have an interest in the restraint is irrelevant.

Therefore, creditors' rights in relation to a merger appear to be subject to transferability as a default's rule. The plain meaning of the words 'in accordance with the provisions of the amalgamation or merger agreement or any other relevant agreement'[130] ('the wording of s 116(7)') indicates that the presumption of transferability of a 'property' may only be restricted by the agreement or a pactum *clearly drafted* in the creditors' contract and *expressly triggered* by a merger. Creditors who do not have an airtight contract with the merging companies will have their rights protected according to the type of the pactum, the nature of the contract and their interest or not in the pactum being effective. Such a rule is highly subjective as the rule of prejudice includes an open notion. Furthermore, the wording of s 116(7) provides full protection when creditors are either protected by the agreement or a clear pactum. The former is unlikely to occur since it would imply that shareholders are looking after the interests of creditors in the implementation of the merger. Although this is not impossible, I hardly see a rationale behind such demeanour since both parties do not have the same interests at stake (not always). It would mean that the merging companies have the 'right' to voluntarily include or exclude certain assets/liabilities from the merger, exposing the creditors of the disappearing company to potential abuse.[131] As creditors cannot attend the special resolution nor voting of the merger, the wording 'in accordance with the merger or amalgamation agreement' will not serve the purpose of protecting their rights. In case of a vague pactum, judicial intervention would be necessary to determine whether the pactum is effective. Balancing the cost of proceedings with the interests or rights disputed will become critical for creditors. Some creditors might not have the financial means to sustain a judicial intervention and therefore not be inclined to dispute whether the pactum contained in their contract allows for transferability.

III- THE SOLVENCY AND LIQUIDITY TEST ('TEST')

[129] [1940] AC 1014 (HL). See also JA Kunst, P Delport & Q Vorster *Henochsberg on the Companies Act* Vol 1 (2006) 639.
[130] S 116(7) of the Act.
[131] MF Cassim (part 1) op cit note 8 at 6.

Like Canadian law,[132] the Act requires the board of each merging company to consider whether the merged company would satisfy the Test upon implementation of the agreement and,[133] if it does reasonably so believe, it may submit the agreement for consideration at a shareholder meeting.[134] It serves essentially to promote the protection of creditors having financial gain at stake in case the merged company is excessively exposed to financial reduction upon implementation of the merger.

(a) The balancing effect

If the board after the Test do reasonably believe that the merged company will become insolvent, it relocates the focus on their fiduciary duties. The board now owes its fiduciary duties to creditors,[135] and must act on behalf of the latter, at least when shareholders and creditors' interests are competing.[136] But this is not always easily doable in a merger.

Within a company set of financial creditors, interests are not identical considering the type of creditors. Financial creditors, employees, secured lenders, etc. are not equally exposed to the same consequences stemming from a merged company being insolvent or not on implementation of the merger. In the board's application of the Test, which creditors do they have to consider? Section 4 of the Act also states that for a company to satisfy the Test, it should be able to pay its debt when they come due (*usually for a period of twelve months*). What are the provisions for a merged company which does not have any claim payable for a period of twelve months but instead for a period of 36 months? What if the number of creditors having their claims protected by the Test is insignificant compared to the number of creditors not having their claim falling within the Test period? These questions show the limited balancing effect of the Test and the area not covered by the board's decision to terminate or not the transaction. In my opinion, the twelve months period is *too short* and *not inclusive* of all types of creditors. Because a merger is a fundamental transaction[137] that has important economic repercussions in SA, considering the financial stability of merged companies for a

[132] S 185(2) of the CBCA.
[133] S 113(4)*(a)* of the Act.
[134] S 113(4)*(b)* of the Act.
[135] Deborah A. DeMott op cit note 106 at 215.
[136] Ibid at 214. See also *Wood v. Dummer* 30 F. Cas. 435 (D. Me. 1824) at 436–47; *Credit Lyonnais Bank Nederland v Pathem Communications Inc* No. CIV. A. 12150, 1991 WL 277613 (del. Ch. Dec. 30, 1991) at 34.
[137] Chapter 5 of the Act, which is headed 'Fundamental Transactions, Takeovers and Offers'. Part A contains sections that deal with proposals for amalgamation or merger (s 113); implementation of amalgamation or merger (s 116).

longer period (36 months) would have been ideal and more inclusive of the various categories of creditors.

Nevertheless, the Test is the only statutory requirement with direct impact on creditors' rights. It helps balancing the fiduciary duty initially owed to shareholders with the interest of creditors vested in the existence and operation of the business of the company. It shifts the first 'recipients' of directors' fiduciary duties merely by increasing the probability that the board's decisions will be justified as business judgments, thereby protecting decisions that might not favour shareholders' rights in implementing a proposed merger, as evidencing undue favouritism toward creditors and undue risk-aversion at the creditors' behest.[138]

[138] Deborah A. DeMott op cit note 106 at 215.

SECTION V: HYBRID PROTECTION

As discussed in section III and IV, the Act made explicit provisions that protect respectively the interests of minorities, majorities and creditors in implementing a merger. However, based on the far-reaching consequences of a merger, there are provisions that appear to shield and balance these stakeholders' interests irrespective of who invoked them.

This section analyses the balancing effects existing in remedies that *do* have one purpose for two entities: protection of shareholders (majorities and minorities) and creditors at the same time.

I- THE DIRECTORS' UNILATERAL POWER TO ABANDON/TERMINATE THE MERGER

This protection does not exist in the Act and could be an area where SA could look to the US. Such protection is referred to as the board of directors' unilateral power to abandon/terminate the merger/amend the agreement. It is general practice for agreement in North American legislation[139] to include that protection.[140] In so doing, directors may vindicate their decisions by proving that the merger lost its appeal, or, when it is faced with some unexpected or material legal proceedings.[141] For instance, the financial 'precarity' of the merged company may be detrimental for its shareholders when it has to tender a substantial number of dissenters. This reduces the company resources, which incidentally impact on its ability to pay its debt within twelve months. The latter highly exposes creditors with immediate claims and could lead directors to cancel the merger considering the company's interests. The 'interest of the company' encompasses the rights and interests of either the shareholders or either the creditors as a whole. Delaware Chancery Court in *Credit Lyonnais Bank Nederland Pathem Communications Inc.*,[142] held that, before the point of actual insolvency '…a board of directors is not merely the agent of the residue risk bearers, but owes its duty to the corporate enterprise'.[143] The word 'enterprise' used in this case includes both creditors' and shareholders' interests.[144] This explains why such power serves to protect both parties.

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[139] S 251(d) of the Delaware General Corporation Law, 2001. See also s 183(6) of the CBCA.
[140] MF Cassim (part 1) op cit note 8 at 17.
[141] Robert W Hamilton *The Law of Corporations in a Nutshell* 5 ed (2000) at 629–630.
[142] *Credit Lyonnais Bank Nederland* supra note 136.
[143] Ibid at 34.
[144] Deborah A. DeMott op cit note 106 at 215.

In the Act, the closest similarity with that power is contained in the wording of s 113(4) with the requirement to satisfy the Test upon implementation of the merged company. This requirement needs to be satisfied prior to the merger resolution and approval. If directors do not so reasonably believe, it is likely that the agreement will never be submitted for approval and the merger will be terminated/abandoned. *Directors are only vested with such power prior to the approval and not post approval or irrespective of it.*

Another similarity exists in the wording of s 115(5)*(b)* of the Act. It is only triggered when the merger resolution was opposed by at least 15 per cent of holders of voting rights.[145] However, s 115(5)*(b)* does not expressly mention 'directors' but rather 'the company' as being the one entitled to decide upon the nullity of the merger resolution. Thus, the company's power to nullify the merger is subject to the main condition of the merger resolution falling within the scope of a mandatory court's approval. *Until the resolution is not disapproved by at least 15 per cent of the holder of voting rights, the company appears not to be able to nullify it.*

Despite the absence of statutory provisions in the Act, directors of companies are permitted to terminate and abandon a merger, *albeit not unilaterally*, under specific circumstances explained above. The board decision to terminate/amend the agreement takes place after consideration of the rights and interests of creditors and shareholders.

III- THE CONTROVERSIAL MEANING OF 'UNFAIR' AND 'OPPRESSIVE'

Sections 115, 163, 164 discussed above expressly provide for the impugned act (in this context would refer to a merger) to be 'unfair' or 'oppressive' to the plaintiff to trigger a court reviewing, a relief and an appraisal. However, no statutory definition of these terms has been provided, which leaves uncertain every remedy in which they have to be proven for the protection of a specific party's rights.

Canadian courts have tried to implement an approach that considers the actual expectations of shareholders as a whole, and where those expectations have been thwarted by the conduct of the majorities' leading to prejudice for minorities when considering if the proposed act will be 'unfair' or 'oppressive'.[146] In that jurisdiction, unfair or oppressive conduct also includes

[145] S 115(3)*(a)* of the Act.
[146] Philip Anisman op cit note 59 at 93.

conduct in any type of 'going private transaction' from the majorities that tends to force the minorities out of the company.[147]

I infer that the concepts of 'unfairness' and 'oppressiveness' appear as a hybrid protection and an effective balancing tool because, unless one of them exists and is evidenced, the impugned act will not be void. Both concepts operate as 'double-edged sword' for majorities, minorities and creditors at the same time. They may protect minorities' and creditors' rights when the impugned merger *includes conduct* that unfairly disregards their interests. On the contrary, they may consolidate the majority's rule and allow for the enforceability of the impugned merger when a complainant *fails to evidence* their 'existence'. Accordingly, the major difficulty with these concepts is in giving them an express definition that will easily lead to certainty for their courts' assessment.

[147] Ibid at 99.

SECTION VI: CONCLUSION

The aim of this research was to identify the measures for protection of minorities, majorities and creditors rights, and to critically assess their fairness considering their level of exposure in implementing a merger. In answering this question, a critical analysis of all the remedies pertaining to protect each party was undertaken. When relevant, US and Canadian legislation and cases were referred to consider whether SA achieves the benchmark to ensure a reasonable balancing of the different stakeholders' interests. In this section, the main findings and recommendations for a 'better' balancing effect of the relevant remedies are made.

I- FINDINGS AND RECOMMENDATIONS

The main findings are that some protections are not properly balanced in consideration of the aforementioned parties' interests. These include the appraisal, the agreement and the oppression remedy — between minorities and majorities — and the creditors' notification coupled with the court review, the open transferability of creditors' contracts and the Test — between majorities and creditors — which in some aspects offers uncertainty in protecting their applicants. The approach adopted in *Black & Decker* and *Loeb, set out in section 2 above, emphasises the importance of policy considerations which must meet the stated goals of s7 of the Act.*

The aim of this research was to analyse whether a balanced approach between minority and majority shareholders rights and thereafter creditors rights – has been achieved. I have identified certain general and specific protections for minorities and creditors. The appraisal is a new and vital 'balancing' measure in s 164 of the Act. I have focused on this and I have concluded that the current appraisal may not fulfil this role adequately. A 'fairer' appraisal that balances the interests of majorities and minorities could be reached in two ways. First, through an extension of the appraisal to absentee shareholders under specific circumstances, and through recognition of partial dissent under specific circumstances to trigger partial appraisal for a specific class of shares for dissenters.

The research also argued that a 'fairer' approval could counterbalance the power of dominant majority by allowing a higher quorum (75 per cent of shareholders with voting rights) and authorising separate class votes to increase the protection of minorities of that class who sometimes represents the numerical majority.

The agreement, although offering equal disclosure of information to shareholders, also offers limited balancing protection. Like in the US, submitting it to an external expert report could provide a more balanced protection of minorities' and majorities' interests. Such express external assessment could reduce a scenario in which majorities might have influenced the board to submit a 'biased' agreement for approval.

The oppression remedy ('relief') balances properly the majority's rule by imposing on majorities a duty to act fairly on behalf of all of the shareholders. However, the openness contained in the test for valuation of shares under the relief and the appraisal is uncertain. Therefore, it equally exposes minorities and majorities interests. Depending on the court's findings and the market value, the valuation could be lesser or higher than the company's offer.

Turning to the creditors' protection, I analysed whether a balanced approach between majorities and creditors' rights exists. I found that the creditors' notification is significant because it is submitted to targeting considerations qua creditors and qua claims before unlocking its judiciary power to have the court looking at the merger and deciding whether to grant leave.[148] The court's room for interpretation and discretionary power into granting or not granting leave offers a 'fair' assessment of shareholders and creditors' interests.
The open transferability of creditors' contracts also offers a balanced approach because it is not absolute as demonstrated in the wording of s 116(7) of the Act. In case of a vague pactum, transfer of liability takes place *only after* the court's careful consideration of the type of the pactum, the nature of the contract, and creditors' interest in the pactum being effective.

The Test helps balancing the fiduciary duty initially owed to shareholders with the interest of creditors vested in the existence and operation of the business of the company, which appears to be a good tool in striking a fair balance between both parties' interests. However, the twelve months' period seems too short to consider the various types of creditors and their interests. Based on the special nature of merger in the Act (a fundamental transaction), a specific merger-related-Test considering a 36 months period could have had a broader inclusion of creditors interests and a more balanced effect.

[148] S 116(1)*(c)* of the Act.

Section V discussed the existence of hybrid protection for shareholders and creditors and suggested that SA includes in the Act a specific statutory power to the board to unilaterally terminate/cancel the merger/amend the agreement inspired from the company law regime in North American legislation.[149] This could provide a 'fairer' protection by relieving the board from the pre-requisite of ss 113(4) and 115(5)*(b)* of the Act.

In conclusion, the research has identified the strengths and weaknesses of the measures introduced in the Act which protect the minorities, majorities and creditors' interests in the context of a merger. The merger provisions do not satisfy entirely the policy aims of the Act identified in the research report. The best way to ensure their alignment may be to amend the legislation and to incorporate some of the provisions discussed from the US and Canada which bring better certainty to the merger process.

[149] MF Cassim (part 1) op cit note 8 at 17.

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