Private M&A

Contributing editors
Will Pearce and John Bick

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GETTING THE DEAL THROUGH

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Private M&A 2019

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Second edition

Getting the Deal Through is delighted to publish the second edition of *Private M&A*, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Brazil, Costa Rica, Ecuador, Egypt, Indonesia, Malaysia, Myanmar, Philippines, Singapore and Taiwan.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Will Pearce and John Bick of Davis Polk & Wardwell, for their continued assistance with this volume.

GETTING THE DEAL THROUGH

London
September 2018

South Africa

Charles Smith and Jutami Augustyn

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Structure and process, legal regulation and consents

1 How are acquisitions and disposals of privately owned companies, businesses or assets structured in your jurisdiction? What might a typical transaction process involve and how long does it usually take?

In South Africa, acquisitions and disposals of privately owned companies are more often structured as share sale transactions (unless the buyer wants to select which assets it acquires and which liabilities it assumes (see below)).

Acquisitions and disposals of privately owned companies have also historically been structured as an issue of shares in the target company coupled with a share repurchase whereby the target company issues new shares to the 'buyer' and repurchases shares held by the 'seller' (ie, the existing shareholder or shareholders). However, given that this transaction structure is the subject of increased and ongoing scrutiny by the South African Revenue Service, it has become less popular.

Another way to structure an acquisition or disposal is by way of a statutory merger or amalgamation pursuant the Companies Act, 2008 (the Companies Act), which allows for the merger of one entity into another or the amalgamation of two entities into a new entity. Implementing an acquisition of a company by way of a statutory merger or amalgamation will result in the combination of all of the assets and liabilities of the merging entities into a single company. The parties are not at liberty to select which assets and liabilities form part of the resultant merged entity.

Where a buyer would like to avoid acquiring a target company in its entirety, with all of its disclosed and undisclosed liabilities, the buyer may opt for an acquisition of the business or assets of the target company. The parties will typically enter into a sale of assets or sale of business agreement in terms of which the buyer agrees to acquire the assets of the target company it wishes to acquire and assume the liabilities of the target company that it wishes to assume, in each case, on the terms and subject to the conditions, as set out in the sale of assets or business agreement. This transaction structure is more complex than a share sale transaction by virtue of the fact that the acquisition agreement will have to deal with each type of asset that is being acquired and each type of liability that is being assumed by the buyer. The parties would also need to take into account relevant labour law provisions. On the other hand, it offers the advantage of allowing the buyer to select the assets and liabilities that will be transferred, instead of acquiring the entire company with all of its assets and liabilities, as would be the case in a share sale transaction or a statutory merger or amalgamation.

The transaction process and the length of time will depend on a number of factors, including:

- which of the above methods is used to effect the transaction;
- the number of parties involved;
- the extent to which the transaction is negotiated; and
- whether any governmental approvals are required for the transaction (eg, competition or antitrust approvals, exchange control approvals or industry-specific approvals and depending on the nature of the transaction (eg, whether there is a change of control)).

2 Which laws regulate private acquisitions and disposals in your jurisdiction? Must the acquisition of shares in a company, a business or assets be governed by local law?

The Companies Act (read with the regulations thereto) is the key piece of legislation regulating acquisitions and disposals of South African companies and their assets or businesses. There are a number of other statutes and regulations that may be relevant to private M&A, including:

- the Exchange Control Regulations, which are enforced by the Financial Surveillance Department of the South African Reserve Bank;
- the Labour Relations Act, 1995 (the Labour Relations Act), which provides, among other things, that the buyer is required to employ the transferring employees on terms and conditions that are on the whole no less favourable to what they enjoyed with the seller;
- the Competition Act, 1998 (the Competition Act), which requires M&A of a certain size to be approved by the relevant competition authorities; and
- certain industry-specific laws and regulations, for example, in the banking, mining and communications sectors.

Transaction agreements are typically governed by South African law. However, subject to compliance with the above laws and regulations, parties are generally free to choose the laws of any other jurisdiction as the governing law of the transaction agreements.

3 What legal title to shares in a company, a business or assets does a buyer acquire? Is this legal title prescribed by law or can the level of assurance be negotiated by a buyer? Does legal title to shares in a company, a business or assets transfer automatically by operation of law? Is there a difference between legal and beneficial title?

Under South African law, there is a distinction made between beneficial owners of shares and the registered holders of shares (otherwise known as nominees). A registered holder of shares is the person whose name appears on the company's securities register, while a beneficial owner is the person entitled to exercise the rights attached to a share (the right to receive dividends, or the right to exercise, or cause to be exercised, the voting rights in relation to the share).

The Companies Act defines a 'shareholder' as the person whose name appears on the company's securities register (ie, the registered holder of the shares) and so the general rule is that the right to vote at shareholders meetings and the right to receive dividends resides with the registered holder and not the beneficial owner. This is subject to two caveats: first, the registered holder is required to exercise those rights in accordance with the instructions of the beneficial owner; and, second, the beneficial owner may vote at a shareholders meeting if its beneficial interest includes the right to vote and the beneficial owner's name appears as the holder of a beneficial interest on the company's register of disclosures, which is a separate register to the securities register.

While in a sale of shares transaction, the buyer acquires the beneficial interest in those shares as a matter of law, the buyer must additionally ensure that it is also registered in the company's register at the closing of the transaction so that it becomes both beneficial owner and registered holder of the shares.

Importantly, a sale of shares is a distinct juristic act from the transfer of beneficial ownership in those shares, which means that notwithstanding the existence of a valid sale of shares agreement, beneficial ownership will transfer only if the seller is the owner of the shares. It is therefore common for the seller to warrant and represent that it has valid title to the shares that are being sold.

4 Specifically in relation to the acquisition or disposal of shares in a company, where there are multiple sellers, must everyone agree to sell for the buyer to acquire all shares? If not, how can minority sellers that refuse to sell be squeezed out or dragged along by a buyer?

The general rule in the case of a private company is that all shareholders must agree to sell their shares for a buyer to aquire all of the compay's shares. However, the Companies Act contains a statutory squeeze-out procedure. The statutory squeeze-out is available only if the target company (including a private company) is a 'regulated company' as contemplated in the Companies Act (ie, a company in which more than 10 per cent of its issued shares have been transferred in the preceding 24 months; or whose memorandum of incorporation (being its constitutional document) expressly provides that the takeover regulations of the Companies Act apply to it). Where this is the case, the buyer may consider a minority 'squeeze-out' in terms of section 124 of the Companies Act. Under section 124 of the Companies Act, if an offer for the target company has been accepted by 90 per cent of the target company's shareholders (excluding the buyer) within four months, the buyer may, within two months, compulsorily purchase the remaining 10 per cent of shares from the minority shareholder or shareholders who did not accept the offer.

It is not unusual for a private company's memorandum of incorporation or shareholders' agreement to contain a 'drag-along' provision pursuant to which minority shareholders are, subject to certain conditions, forced to sell their shares along with a majority shareholder. This is not a statutory provision, but is nevertheless a regular provision in private company memoranda of incorporation and shareholders' agreements.

If the minority shareholders do not agree to sell and the company's memorandum of incorporation or shareholders' agreement does not contain a 'drag-along' provision, the transaction may be structured as a scheme of arrangement. If approved by disinterested shareholders representing at least 75 per cent of the voting rights attached to the company's shares exercised on the transaction resolution, the scheme will be binding on all of the shareholders, including the minority shareholders. Schemes are, however, more often used in public M&A transactions and are rarely utilised in private M&A transactions.

5 Specifically in relation to the acquisition or disposal of a business, are there any assets or liabilities that cannot be excluded from the transaction by agreement between the parties? Are there any consents commonly required to be obtained or notifications to be made in order to effect the transfer of assets or liabilities in a business transfer?

Parties in a sale of business or sale of assets are, subject to certain caveats, free to choose which assets or liabilities, or both, are transferred to the buyer as part of the transaction.

In terms of section 197 of the Labour Relations Act, where a business is transferred as a going concern, the employees of the target company are automatically, by operation of law, transferred to the acquiring entity on the same terms and conditions of employment, and the acquiring entity is automatically substituted as their new employer. The Labour Relations Act allows for parties to contract out of this position provided that an agreement to that effect is entered into between the buyer, the seller and the affected employees (or their representatives or trade union).

South African law also contains certain default provisions with respect to liability for environmental matters (eg, contamination and pollution) that need to be considered.

6 Are there any legal, regulatory or governmental restrictions on the transfer of shares in a company, a business or assets in your jurisdiction? Do transactions in particular industries require consent from specific regulators or a governmental body? Are transactions commonly subject to any public or national interest considerations?

As a general rule, there are no restrictions on foreign investments in South Africa. There are also no restrictions on the transfer of shares in a company or on the transfer of a company's business or assets. However, certain specific industries (including mining, banking, insurance and broadcasting) have specific statutory or policy restrictions on the percentage of shareholding in a South African company. In addition, South Africa has exchange control regulations that require any outflow of capital or any inflow of loan funds into South African to be preapproved by the South African Reserve Bank. Accordingly, a South African resident cannot transfer any shares to a South African non-resident (and vice versa) without South African Reserve Bank approval, nor can a South African non-resident advance a loan into South Africa without South African Reserve Bank approval. Approval is usually given, provided that the South African Reserve Bank is satisfied that fair consideration for the shares has been received in South Africa or that the loan is on an arms-length basis (based on certain policy thresholds).

If a proposed transaction constitutes a 'merger' under the Competition Act and meets certain prescribed monetary thresholds, the competition authorities must be notified of the proposed transaction. In assessing the proposed transaction, the competition authorities are required, under the Competition Act, to consider the effect of the proposed transaction on the 'public interest'. The 'public interest' includes, inter alia, the effect of the proposed transaction may have on:

- a particular South African industry or region;
- employment;
- the ability of small businesses or firms controlled or owned by historically disadvantaged individuals to become more competitive; and
- the ability of national industries to compete in international markets.

In addition, in terms of proposed amendments to the Competition Act, it is intended that the public interest factors will be broadened or amended as follows:

- the amendment being to the third bullet above, which it is proposed will read: the ability of small and medium businesses, or firms controlled or owned by historically disadvantaged persons, to effectively enter into, participate in and expand within the market; and
- the introduction of a new public interest factor, being the promotion of a greater spread of ownership, in particular to increase the levels of ownership by historically disadvantaged persons and workers in firms in the market.

Moreover, a further proposed amendment to the Competition Act (see 'Update and trends') contemplates allowing the South African National Executive to take into account national security interests in respect of acquisitions by foreign firms.

Notwithstanding that a proposed transaction may not meet the monetary thresholds for a mandatory notification to the competition authorities ('small mergers'), the Competition Act empowers the Competition Commission to request (within six months of implementation of the transaction) that the parties formally notify it of the transaction.

7 Are any other third-party consents commonly required?

There are no general third-party consents prescribed by law in respect of a transfer of shares. However, as stated in question 6, certain specific industries have statutory restrictions that may require the consent of a regulator or government authority for a transfer of shares.

It is not uncommon for private company memoranda of incorporation or shareholders' agreements to contain some sort of pre-emptive right or other provision requiring a selling shareholder to obtain the consent of other shareholders in the company before transferring its shares to a third party.

It is also not uncommon for agreements with third parties to require consent for a change of control in respect of a target company. Accordingly, the parties may require the prior consent of certain key lenders, lessors, suppliers and customers if the proposed transaction triggers such a change of control consent.

In the context of a sale of a business or assets, while assets can generally be freely transferred to a buyer without the need for any third-party consents, liabilities can only be transferred with the prior consent of the person to whom such liability is owed. Accordingly, the consent of third-party counterparties will be required to assign a contract in its entirety. In addition, certain agreements might explicitly require consent before any rights or obligations under an agreement may be transferred to any other party.

8 Must regulatory filings be made or registration fees paid to acquire shares in a company, a business or assets in your jurisdiction?

Depending on the nature of the transaction, approvals may be required from one or more of the following regulatory bodies:

- the Competition Commission in respect of small and intermediate mergers, or the Competition Commission and the Competition Tribunal in respect of large mergers (a statutory filing fee is payable in respect of both intermediate and large mergers);
- the South African Takeover Regulation Panel in respect of transactions involving a 'regulated company' (see question 4) (a fee will be payable);
- the South African Reserve Bank, where the transaction involves a South African non-resident party and requires exchange control approval (no fee will be payable), and the National Treasury (no fee will be payable) if the transaction is not within an established exchange control policy; and
- the relevant sector-specific regulator, if applicable (a fee may be payable).

Transfer taxes, in the form of securities transfer tax (STT), are payable in respect of a disposal of shares. For shares in an unlisted South African company, STT is payable by the target company at a rate of 0.25 per cent of either the sale consideration or the market value of the shares (if the sale consideration given is less than the market value of the shares) but may be recovered by the target company from the buyer. Certain exemptions from STT may also be available.

Advisers, negotiation and documentation

9 In addition to external lawyers, which advisers might a buyer or a seller customarily appoint to assist with a transaction? Are there any typical terms of appointment of such advisers?

Depending on the complexity of the transaction and their respective in-house capacity, parties generally appoint a financial adviser and accountants to assist with the transaction. Financial advisers provide strategic and valuation advice, while accountants assist with accounting and financial diligence matters. Accountants and lawyers are often engaged to provide tax-structuring advice and to assist with tax diligence. Strategy and business consultants may also be appointed to conduct commercial due diligence. In addition, if the transaction triggers the requirement for an independent fairness opinion or an independent expert's report, the parties may need to appoint a person who meets the requirements for an independent expert (typically an investment bank or accounting firm not involved in the transaction).

Most professional advisers have standard terms of engagement. Fees will typically depend on the complexity and value of the deal, timelines and the nature of any required work product. A buyer's financial, accounting and legal fees may add up to several per cent of the deal value.

10 Is there a duty to negotiate in good faith? Are the parties subject to any other duties when negotiating a transaction?

The South African law of contract does not impose a general duty to negotiate in good faith. Accordingly, the general rule is that parties to a transaction are permitted to pursue their own self-interest. In recent years, however, there has been increased emphasis on the role of good faith, public policy and constitutional values of fairness and reasonableness in determining whether a contractual term will be upheld by a court. The test for whether a contractual term can be overridden on the grounds of public policy now involves two questions: first, whether the clause itself is so manifestly unreasonable as to offend public policy (which, under the Constitution, imports the notions of fairness, justice and reasonableness); and, second, whether the clause should be enforced in the light of the particular circumstances of the case and relative bargaining power of the parties. This is a nascent area of the law that is still developing, however, and the extent to which courts will interfere with contractual undertakings negotiated by sophisticated parties outside the consumer context remains to be seen.

11 What documentation do buyers and sellers customarily enter into when acquiring shares or a business or assets? Are there differences between the documents used for acquiring shares as opposed to a business or assets?

In a sale of shares transaction, the main transaction agreement will be a sale of shares agreement in terms of which the seller agrees to transfer its shareholding in the target company to the buyer on the terms, and subject to the conditions, set out in the sale of shares agreement.

In a sale of assets or a sale of business transaction, the parties will typically enter into a sale of assets or sale of business agreement in terms of which the buyer agrees to acquire the assets of the target company it wishes to acquire, and assume the liabilities of the target company that it wishes to assume, in each case on the terms, and subject to the conditions, set out in the sale of assets or business agreement.

The following agreements may be applicable to both share sale transactions and asset or business sale transactions:

- the buyer may deliver a non-binding expression of interest in which it expresses its desire to acquire the target shares or the target business or assets, and proposes indicative terms for the transaction;
- the parties may enter into an exclusivity agreement pursuant to which the seller agrees not to solicit a competing offer from a third party in respect of the target shares or the target business or assets;
- the parties may enter into a non-disclosure agreement in terms of which each party undertakes not to disclose information relating to the proposed transaction and not to disclose any confidential information received as part of the due diligence process or in negotiating the transaction agreements;
- the parties may enter into a disclosure letter in terms of which the seller makes certain disclosures against which the warranties in the sale of shares agreement or the sale of business or assets agreement (as applicable) are qualified; and
- at closing, the parties will need to sign certain documents to transfer or register title to the sale shares or assets. These will differ depending on the nature of the assets being transferred (eg, for a transfer of shares, transfer forms will need to be signed and new share certificates issued).

12 Are there formalities for executing documents? Are digital signatures enforceable?

There are generally no formalities for executing documents in South Africa. In most instances, a signature by a duly authorised signatory will suffice. However, certain documents, such as mortgage bonds, affidavits and agreements relating to the transfer of immovable property, require certain formalities to be complied with in order to be valid (eg, being signed in the presence of a commissioner of oaths).

In terms of the Electronic Communications and Transactions Act, 2002, digital signatures are generally enforceable, although certain agreements may not be concluded electronically. Furthermore, parties may agree any stricter standards for signature should they so wish.

Due diligence and disclosure

13 What is the typical scope of due diligence in your jurisdiction? Do sellers usually provide due diligence reports to prospective buyers? Can buyers usually rely on due diligence reports produced for the seller?

In the context of South African private M&A transactions, it would be unusual to proceed with a transaction without having first completed a high level legal and financial due diligence exercise so as to give the buyer a level of comfort regarding the assets that are the subject of the transaction and to identify any risks that would need to be mitigated by way of additional warranty and indemnity cover. The scope of due diligence varies from deal to deal depending on the specific requirements of the buyer. In South Africa, buyers tend to opt for a limited scope 'red flags only' due diligence that seeks to confirm title to the shares or assets that are the subject of the transaction; identify any change of control provisions in material contracts that may be triggered by the proposed transaction; and identify any material undisclosed risks and liabilities.

In the context of a controlled auction process, it is not uncommon for the successful bidder (and its funders for purposes of the proposed transaction) to be given reliance on the due diligence report prepared on behalf of the vendor. However, liability is usually limited to loss arising from the negligence of the person that prepared the report only.

14 Can a seller be liable for pre-contractual or misleading statements? Can any such liability be excluded by agreement between the parties?

A party induced to enter into a contract by a material pre-contractual misstatement intended to induce it to enter into the contract can use a restitutionary remedy to either uphold the contract or claim restoration of any performance that has been made in terms of the contract. Liability for misrepresentation can, however, be excluded by agreement between the parties (for example, by way of an 'as is' clause).

Furthermore, a party may be liable under the law of delict (tort) for any fraudulent or negligent misrepresentation that induces the buyer to enter into the agreement. While negligent misrepresentations may possibly be excluded by agreement between the parties, parties cannot contract out of liability for fraudulent misrepresentation.

15 What information is publicly available on private companies and their assets? What searches of such information might a buyer customarily carry out before entering into an agreement?

Publicly available information on private companies in South Africa is relatively limited. Accordingly, it is unusual for prospective buyers to enter into definitive transaction agreements without having completed some level of diligence (unless the transaction agreements themselves are conditional on the completion of a due diligence).

South African private companies are required to register with the Companies and Intellectual Property Commission (CIPC). The publicly available information held by the CIPC is relatively limited and includes elementary details such as registration dates, directors' names and addresses, and financial year end. No details are provided on a company's assets or its shareholding. Copies of a company's constitutional documents may also be uplifted from the CIPC, although requesting and obtaining this is currently still a time-consuming process. The CIPC is, however, in the process of rolling out an automated system to obtain copies of documents filed with the CIPC.

In addition, any person can, in terms of the Promotion of Access to Information Act, 2000 request documents from a private body, provided that such person follows the relevant procedural steps in requesting the information and can show that it requires the information in order to exercise or protect a right. There may, however, be grounds for refusing such access to a requested documents (or part thereof), for example where information is in fact confidential or where information amounts to personal data.

16 What impact might a buyer's actual or deemed knowledge have on claims it may seek to bring against a seller relating to a transaction?

As a general principle, a party's actual or deemed knowledge will not preclude it from bringing a claim for breach of a warranty (unless the agreement expressly provides that actual or deemed knowledge precludes such a claim). However, where a buyer enters into an agreement in manifest bad faith (eg, knowing that a particular set of circumstances exist, which the other party is unaware of, that would make a warranty untrue) a court may refuse to enforce the claim on the basis that to do so would be inimical to public policy (see question 10).

Pricing, consideration and financing

17 How is pricing customarily determined? Is the use of closing accounts or a locked-box structure more common?

Closing accounts and locked-box structures are used in private in South African private M&A transactions, with locked-box structures being the more common of the two, particularly in the context of private equity transactions.

18 What form does consideration normally take? Is there any overriding obligation to pay multiple sellers the same consideration?

Consideration in South African private M&A transactions often takes the form of cash, shares or a combination of both.

There is no obligation to pay multiple sellers the same consideration. However, if the acquisition is structured as a scheme of arrangement or as a 'squeeze-out' in terms of section 124 of the Companies Act (see question 4), the buyer may be required to pay the same consideration to each of the sellers.

19 Are earn-outs, deposits and escrows used?

Escrow arrangements are not uncommon in South African private M&A transactions. Deposits are unusual, and earn-outs are most commonly used in the context of management buyout transactions.

20 How are acquisitions financed? How is assurance provided that financing will be available?

Bank-led acquisition or leverage financing from financial institutions are the most commonly used methods of financing private M&A transactions in South Africa. It is also not uncommon for buyers to take out some form of bridge loan to finance an acquisition and then to repay the bridge funding, post-transaction, by way of a high-yield bond offering or (in the case of a publicly listed buyer) a rights offer.

Sellers are often provided comfort of the buyer's certainty of funds through some form of escrow arrangement, bank guarantee or letter of support from a lender. The ultimate method chosen to provide certainty of funds to a seller often depends on the nature of the transaction, the identity of the buyer and the quantum of the purchase price.

21 Are there any limitations that impact the financing structure? Is a seller restricted from giving financial assistance to a buyer in connection with a transaction?

In South Africa, a target company may provide financial assistance to buyers in connection with the subscription or acquisition of its own securities if the shareholders of the target company authorises such financial assistance by way of special resolution (more than 75 per cent) and if the board of the target company adopts a resolution confirming that the target company will be solvent and liquid after such financial assistance is granted.

Furthermore, insofar as a related company to the target company provides financial assistance to a buyer, such related company must also obtain the board and shareholder resolutions set out above. A related company would include a subsidiary of a target company, its holding company or a sister company of the target company.

If the seller is a related party to the target company (eg, if it holds all the shares in the target company), the seller will need to pass the same financial assistance resolutions as mentioned above.

Conditions, pre-closing covenants and termination rights

22 Are transactions normally subject to closing conditions? Describe those closing conditions that are customarily acceptable to a seller and any other conditions a buyer may seek to include in the agreement.

Although signing and completion of transactions can occur simultaneously, most transactions will be subject to some form of conditionality. The most common closing conditions include:

- obtaining regulatory approvals (eg, all applicable competition and antitrust approvals, exchange control approvals or industry-specific approvals) (see question 8);
- the necessary resolutions to approve the transaction;
- obtaining all applicable consents from counterparties (including lenders) to material agreements where such material agreements contain change of control or other provisions that will be triggered by the proposed transaction; and
- obtaining all requisite waivers by any remaining shareholders of their pre-emptive rights.

While sellers will want to limit the conditionality of the transaction to the above conditions only, the buyer may require additional conditions such as:

- the absence of a material adverse change;

- a new shareholders' agreement being entered into between the buyer and any remaining shareholders of the target company; and
- transitional services agreements being entered into between the target company and the members of its former group who provided certain critical services to it prior to the transaction.

23 What typical obligations are placed on a buyer or a seller to satisfy closing conditions? Does the strength of these obligations customarily vary depending on the subject matter of the condition?

Both parties are usually required to at least use their reasonable commercial endeavours to ensure that conditions are satisfied. Certain conditions may come with a more onerous obligation to use best efforts to ensure satisfaction of conditions. Although not common, in certain transactions where a seller has sufficient negotiating leverage, they may require the buyer to agree to a 'hell or high water' standard whereby the buyer agrees to take whatever steps necessary to ensure that a condition is satisfied, regardless of the amount of money and effort required. This standard is not common, and is almost invariably used in the context of conditions relating to obtaining competition and antitrust approvals for the transaction.

24 Are pre-closing covenants normally agreed by parties? If so, what is the usual scope of those covenants and the remedy for any breach?

Sellers will typically agree to some form of pre-closing covenants. Such covenants are usually aimed at ensuring that the target company's business is conducted in the ordinary course of business in a manner consistent with past practice; and preserving the value of the target company by prohibiting the seller and the target company from carrying out any actions that are designed to maximise short-term profit but may result in long-term loss to the target company (eg, declaring and paying out of a special dividend or implementing changes to accounting policies). It is, however, important that these covenants do not confer control on certain types of buyers prior to implementation of the transaction, which could give raise to competition and antitrust issues.

25 Can the parties typically terminate the transaction after signing? If so, in what circumstances?

The parties can typically terminate the transaction after signing but prior to closing. However, it is unusual to have a right to terminate after closing and therefore 'unscramble the egg'. The usual grounds for terminating the transaction prior to closing include:

- a material breach of the agreement by one party and a failure to cure such breach after being given a reasonable period to do so;
- an insolvency event;
- an order of court or some other competent government body (eg, the Department of Mineral Resources rejecting an application to transfer a mining right) prohibiting the consummation of the transaction; or
- the occurrence of a material adverse change prior to closing.

The parties can obviously also terminate an agreement by mutual consent at any time.

26 Are break-up fees and reverse break-up fees common in your jurisdiction? If so, what are the typical terms? Are there any applicable restrictions on paying break-up fees?

Break-up fees and reverse break-up fees are not as common in private M&A transactions as they may be in public M&A transactions. Where they are contemplated, parties need to consider whether such a break-up fee or reverse break-up fee, as structured, would constitute financial assistance under section 44 of the Companies Act and thus require shareholder approval and confirmation by the company's board that after paying such fee, the company will remain solvent and liquid.

In addition, to the extent that the target company is a 'regulated company' as contemplated in the Companies Act, our takeover regime prohibits break-up fees in excess of 1 per cent of the deal value. No such cap exists in respect of reverse break-up fees.

Representations, warranties, indemnities and post-closing covenants

27 Does a seller typically give representations, warranties and indemnities to a buyer? If so, what is the usual scope of those representations, warranties and indemnities? Are there legal distinctions between representations, warranties and indemnities?

Sellers typically give warranties and indemnities to a buyer. It is not uncommon for a seller to push back on giving representations. Under South African law, a negligent or fraudulent misrepresentation gives rise to a claim in delict (tort) while a warranty breach will only give rise to a contractual claim. The remedy and quantum of damages will differ between the two.

An indemnity is essentially an undertaking by one of the parties to make good any losses suffered, costs incurred or damages suffered by the other party as a result of the occurrence of a particular event. Where a party claims under a breach of warranty, that party will have to prove its losses. The manner of quantifying claims under an indemnity is usually regulated by agreement between the parties. Indemnities can also be used alongside warranties in South Africa, whereby a party agrees to indemnify the other for any losses suffered, costs incurred or damages suffered by the latter as a result of a breach of warranty by the former. However, sellers are becoming less willing to offer warranties on an indemnity basis.

The scope of the representations, warranties and undertaking are the subject of negotiation and largely depend on the specific type of transaction. While there may be similarities between certain types of transactions, there is significantly more scope for negotiation and the concept of 'market practice' is less developed than in the European and US markets.

28 What are the customary limitations on a seller's liability under a sale and purchase agreement?

Limitations on a seller's liability are usually heavily negotiated between the parties. It is not uncommon for some form of limitation to be agreed. This usually takes the form of one or more of the following:

- limitations as to the time period in which claims may be brought. This may differ between certain types of claims. For instance, claims for breach of 'business warranties' may be limited to three years, while tax warranty claims may be limited to the maximum period in which the applicable tax authority may assess the matter and fundamental warranties such as title to the sale shares may be uncapped;
- a de minimis and 'basket' limitation limiting claims below an agreed amount so as to avoid the inconvenience of trivial claims; and
- an upper limit to the amount that a party may claim. It is not uncommon for parties to agree an upper limit that is equal to the purchase price or some percentage thereof.

While typically most of the limitations referred to above are included, the time and monetary amounts can differ substantially on different types of transactions for the same reasons as those set out in question 27.

29 Is transaction insurance in respect of representation, warranty and indemnity claims common in your jurisdiction? If so, does a buyer or a seller customarily put the insurance in place and what are the customary terms?

Warranty and indemnity insurance is available in South Africa and has been used in a number of transactions, particularly, private equity transactions. It is also becoming increasingly common in South African private M&A transactions, but it is still the exception rather than the norm. The typical approach would be for the buyer to take out the policy.

30 Do parties typically agree to post-closing covenants? If so, what is the usual scope of such covenants?

Post-closing covenants are usually limited to non-compete undertakings and undertakings not to solicit employees, suppliers or customers.

Update and trends

South Africa was the most active M&A country in Africa in the first quarter of 2018, according to Mergermarket statistics.

This aligns with the trend we saw on the ground at the start of the year. At the start of the year, our outlook for M&A, including private M&A, for the remainder of 2018 and moving into 2019, was cautiously optimistic. In our view, the increased private M&A activity in South Africa stemmed from both a global uptick in M&A activity, which affected our market, as well as from a change of leadership in South Africa. Boosting investor confidence into the region significantly, Cyril Ramaphosa became president of the country in mid-February 2018 after Jacob Zuma's resignation, following the demands of the African National Congress party.

As highlighted by Mergermarket, despite the low M&A activity targeting African countries in the second quarter of 2018, outbound M&A activity has picked up again since the first quarter of 2018 with nine deals worth a disclosed US$1.5 billion. South Africa has led the way with five deals making up US$1.1 billion of outbound deal value in the second quarter of 2018. South Africa has recently entered a technical recession, and although we remain cautiously optimistic about M&A in the country, the effect of the technical recession on the market remains to be seen.

From a sector perspective, energy, mining and utilities was the most targeted sector by deal value and count in the first and secon quarters of 2018 (according to Mergermarket statistics), followed by consumer goods and services and business services. As one of the biggest sectors in South Africa, mining and the regulation of this sector continues to be a key focus for developments. Regulation of this sector continues to develop.

Of interest to private M&A investors is that in June 2017, the South African Ministry of Mineral Resources published the much-awaited revision of the Broad-Based Black Economic Empowerment Charter for the South African Mining and Minerals Industry for public comment (Revised Charter). The Revised Charter, among other things, proposes a minimum 30 per cent black ownership requirement for mining rights holders (up from 26 per cent) and proposes elaborate transitional provisions to phase in the minimum 30 per cent target. The ownership requirements applicable to prospecting rights are very context specific. The initial commenting period has elicited huge response in the market and, therefore, there is still a little way to go to finalise the Revised Charter, but the hope is that it will bring much needed policy certainty to this important industry within the South African economy.

An important development from a regulatory competition perspective has been the introduction of the Competition Amendment Bill 23 of 2018 (the Competition Bill), which was first released for public comment in December 2017 and has since been revised. The amendments are expected to come into force before the end of 2018.

The latest round of proposed amendments include extending the mandate of the South African competition authorities so as to address, inter alia, concerns surrounding the high level of concentration and barriers to market entry that prevent small and medium-sized enterprises as well as firms owned by historically disadvantaged South Africans, from effectively participating in the South African economy. In addition, further power is conferred on the South African National Executive. These proposed amendments are as follows: (i) the introduction of provisions that allow for the South African National Executive's intervention in respect of acquisitions by foreign entities that affect the national security interests of South Africa; and (ii) amended and additional public interest grounds focused on the protection of historically disadvantaged South Africans (see question 6 above).

It is also worth mention that South Africa is expecting an amendment to the Companies Act, 2008, which should be published for public comment in the latter part of 2018. While it is not yet certain what they changes will address, it has been suggested that we can expect proposed amendments to address certain technical and procedural matters and possibly some changes to enhance the corporate governance requirements of certain companies.

Tax

31 Are transfer taxes payable on the transfers of shares in a company, a business or assets? If so, what is the rate of such transfer tax and which party customarily bears the cost?

STT is levied on the transfer of a security at a rate of 0.25 per cent. STT is payable by the issuer of the security but may be recovered from the transferee. Transfer duty is payable on the transfer of immovable property in South Africa at varying rates depending on the value of the property. These transfer taxes are subject to various exemptions. Transfers of other business assets are not generally subject to transfer taxes or duties.

32 Are corporate taxes or other taxes payable on transactions involving the transfers of shares in a company, a business or assets? If so, what is the rate of such transfer tax and which party customarily bears the cost?

A person disposing of shares in a company, a business or assets may be subject to capital gains tax (CGT) or income tax (depending on whether the person held the relevant asset as a capital asset or a revenue asset). Generally speaking, companies pay CGT at a rate of 22.4 per cent, trusts at a rate of 36 per cent and individuals at a rate of up to 18 per cent. Conversely, companies pay income tax at a rate of 28 per cent, trusts at a rate of 45 per cent and individuals at a rate of up to 45 per cent.

Value added tax (VAT) is levied (at a rate of either 15 or zero per cent) on the supply of goods and services by registered vendors. Certain supplies are exempt from VAT. Generally, a sale of shares will be an exempt supply for VAT purposes. The sale of a business as a going concern may qualify for 'zero rating' (provided that all of the requirements are met). The person liable to account for VAT will depend on the nature of the supply, the parties to the transaction and where the supply is treated as taking place for VAT purposes.

Employees, pensions and benefits

33 Are the employees of a target company automatically transferred when a buyer acquires the shares in the target company? Is the same true when a buyer acquires a business or assets from the target company?

If ownership in an entity is acquired by way of a share sale transaction, and the entity continues to operate in the same way as before the acquisition of shares, the only change happens at ownership level and there will be no employment consequences arising from the sale. The employees of the target company will remain employees of company subject to their existing terms and conditions of employment. This is different to the position in a sale of a business as a going concern. Where the nature of a transaction is a sale of a business as a going concern, section 197 of the Labour Relations Act applies (see question 5). In this event, the employment contracts of the employees of the target company transfer automatically to the acquiring entity and the acquiring entity is automatically substituted as their new employer. The acquirer is required to employ the transferring employees on terms and conditions that are on the whole no less favourable to what they enjoyed at the old employer, except where these are regulated by a collective agreement (ie, an agreement between the old employer and a trade union), in which event the acquirer must comply with the terms of the collective agreement as they are. The acquirer must recognise the transferring employees' length of service with the old employer.

Where a transaction is structured as an asset sale only (ie, the assets being sold do not constitute a going concern business), section 197 of the Labour Relations Act is not triggered and the employees of the seller do not automatically transfer to the buyer. In this instance, the consent and agreement of the employees' employment contracts to be transferred to the buyer. Because the employment consequences set out in section 197(2) of the Labour Relations Act also apply in the event of the sale of 'part of a business' or 'a service' a careful analysis must be undertaken in order to assess whether the sale of a particular asset may trigger the application of section 197.

34 Are there obligations to notify or consult with employees or employee representatives in connection with an acquisition of shares in a company, a business or assets?

Except to the extent that it is provided for in a collective bargaining agreement, there is no statutory obligation to inform or consult with the employees or recognised trade union or employee representatives in a share sale, asset sale or sale of a business as a going concern. It is, however, recommended, from a good industrial relations perspective, to keep employees and recognised trade union and employee representatives informed of any anticipated change in ownership in the shares of the company, its assets or its business.

35 Do pensions and other benefits automatically transfer with the employees of a target company? Must filings be made or consent obtained relating to employee benefits where there is the acquisition of a company or business?

In the case of a share sale, and where there is a need to transfer employees from the previous holding company's pension fund, provident fund or medical aid to those of the buyer, an amendment to the employees' terms and conditions of employment would need to be negotiated and agreed with the employees or their representatives.

In the context of a going concern business transfer, section 197(4) of the Labour Relations Act provides that employees may be transferred to another retirement fund, provided that the provisions of section 14(1)(c) of the Pension Funds Act of 1956 are complied with. In essence, this means that the Registrar of Pension Funds has to be satisfied that the new scheme is reasonable and equitable and that it accords full recognition to the reasonable benefit expectations of the transferring employees.

In the case of a sale of business, the identity of the participating employer changes. The consequences of a change in employer are dependent upon the rules of the seller's fund, which may allow for the new employer (the buyer) to be substituted in the place of the old employer (ie, the seller), normally subject to the approval of the trustees of the fund. If a substitution is not permitted by the rules, the buyer would need to find a new fund that largely replicates the benefits of the old fund and arrange for the employees' membership of the old fund, together with the assets and liabilities of the old fund that relate to the employees, to be transferred to the new fund in terms of section 14(1)(c) of the Pension Funds Act of 1956.

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