THE Shareholder Rights and Activism Review

Seventh Edition

Editor
Francis J Aquila

THE LAWREVIEWS

THE SHAREHOLDER RIGHTS AND ACTIVISM REVIEW

Seventh Edition

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PREFACE

In the years since the last financial crisis, shareholder activism has been on the rise around the world. Institutional shareholders are taking a broad range of actions to leverage their ownership position to influence public company behaviour. Activist investors often advocate for changes to the company, such as its corporate governance practices, financial decisions and strategic direction. Shareholder activism comes in many forms, from privately engaging in a dialogue with a company on certain issues, to waging a contest to replace members of a company's board of directors, to publicly agitating for a company to undergo a fundamental transaction.

Although the types of activists and forms of activism may vary, there is no question that shareholder activism is a prominent, and likely permanent, feature of the corporate landscape. Boards of directors, management and the markets are now more attuned to and prepared for shareholder activism, and engaging with investors is a priority for boards and management as a hallmark of basic good governance.

Shareholder activism is a global phenomenon that is effecting change to the corporate landscape and grabbing headlines around the world. Although shareholder activism is still most prevalent in North America, and particularly in the United States, activism campaigns directed at non-US companies now represent almost half of global activism activity. This movement is being driven by, among other things, a search by hedge funds for diversified investment opportunities and a cultural shift towards increased shareholder engagement in Europe, Australia and Asia.

Since the fourth quarter of 2021, global activism activity has been at higher levels than the market has seen for a number of years. Looking forward, activism activity is generally expected to remain strong, although events such as the war in Ukraine are having an impact on activity levels in certain jurisdictions. Moreover, shareholder activists are expected to remain focused on environmental, social and political (ESP) considerations and corporate governance.

As shareholder activists and the companies they target continue to be more geographically diverse, it is important for legal and corporate practitioners to understand the legal framework and emerging trends of shareholder activism in the various international jurisdictions facing activism. *The Shareholder Rights and Activism Review* is designed as a primer on these aspects of shareholder activism in such jurisdictions.

My sincere thanks to all of the authors who contributed their expertise, time and labour to this seventh edition of *The Shareholder Rights and Activism Review*. As shareholder activism continues to diversify and increase its global footprint, this review will continue to serve as an invaluable resource for legal and corporate practitioners worldwide.

Francis J Aquila
Sullivan & Cromwell LLP
New York
August 2022

Chapter 12

SOUTH AFRICA

Ezra Davids and Ryan Kitcat[1]

I OVERVIEW

Historically, shareholder activism has not been prevalent in South Africa. More recently, however, shareholder activism has gradually been on the rise, in line with global trends. This increase in shareholder activism can be attributed to a number of factors, including:

a the influence of shareholder activism in other jurisdictions, mainly the United States and Europe;
b a widely held market with an internationalised shareholder base;
c more active ownership and greater calls for accountability in boardrooms by institutional and other investors; and
d a regulatory and corporate governance framework that promotes and creates an enabling environment for shareholder activism or activist-like interventions.

Shareholder activism involves campaigns or proposals by one or more shareholders seeking to effect some change or reform within a company, in relation to its business, governance, management or strategy, or in respect of a particular corporate action or fundamental transaction. Examples of activist proposals seen in South Africa include the following:

a reconstituting the board or replacing a CEO;
b influencing executive remuneration;
c revising corporate strategies;
d addressing operational performance issues;
e pursuing environmental, social and governance (ESG) related agendas;
f making balance sheet proposals, such as returns of capital to shareholders through buy-backs or distributions;
g changing the capital structure or capital allocation strategy;
h monetising assets (e.g., by forcing divestitures or spin-offs); and
i facilitating or frustrating mergers and acquisitions (M&A).

II LEGAL AND REGULATORY FRAMEWORK

The primary sources of law and regulation relevant to shareholder rights and activism are the Companies Act 71 of 2008 (the Companies Act), Chapter 5 of the Companies Regulations 2011 (the Takeover Regulations), the Financial Markets Act 19 of 2012 (the Financial Markets Act) and common law.

1 Ezra Davids is chairman and senior partner and Ryan Kitcat is a partner at Bowmans.

Takeovers and 'affected transactions' such as statutory mergers, schemes of arrangement, and disposals of all or a greater part of a company's assets or undertaking are regulated under Chapter 5 of the Companies Act and the Takeover Regulations. In the context of such transactions, the Takeover Regulation Panel (TRP) is mandated to ensure the integrity of the marketplace and fairness to securities holders, and to prevent actions by offeree companies designed to impede, frustrate, or defeat an offer or the making of fair and informed decisions by securities holders. The TRP has the power to initiate or receive complaints, conduct investigations and issue compliance notices.

The Financial Markets Act provides for the regulation of financial markets and prohibits insider trading and market abuse. The Financial Sector Conduct Authority (FSCA) is responsible for enforcing the Financial Markets Act.[2]

The Listings Requirements of the Johannesburg Stock Exchange (JSE), South Africa's primary exchange, apply to JSE-listed companies. The Listings Requirements regulate, among other things, the fair and equal treatment of shareholders, access to information, voting thresholds for certain corporate actions, and pre-emptive rights and related party transactions.

The King IV Report on Corporate Governance for South Africa 2016 (the King Code), issued by the Institute of Directors South Africa, contains various principles and recommendations intended to promote good corporate governance, many of which are relevant to shareholder rights and engagement. Certain principles in the King Code are incorporated into the Listings Requirements, making it mandatory for JSE-listed companies to comply with them, with the balance of the King Code's principles and recommendations to be implemented on an 'apply and explain' basis.

Additionally, certain other regulatory avenues, although not intended as a means for shareholder activism, indirectly create opportunities for shareholder intervention and engagement. For example, shareholders, acting alone or with other stakeholders, may use the 'public interest' considerations assessed by the competition (antitrust) authorities as part of the merger approval or clearance process as a means to delay or thwart a transaction.

Some of the legal and regulatory avenues for shareholder activism are set out below.

i Ability to influence shareholders' meetings and approvals

Shareholders are entitled to attend, speak at and vote at a meeting, either themselves or via proxy. This allows shareholders to ask difficult questions of directors, express their views or lobby support from other shareholders for a particular agenda (e.g., a 'vote no' campaign). Activists will often push their agendas at general meetings and in mainstream and social media.

Shareholders have the ability to requisition a shareholders' meeting by delivering signed demands to the company, specifying the purpose for which the meeting is proposed. If the company receives, in aggregate, demands from holders of at least 10 per cent of the voting rights entitled to be exercised in relation to the matter proposed, it must call a meeting unless the company or another shareholder successfully applies to court to set aside the demand on the grounds that it seeks only to reconsider a matter that has already been decided by shareholders, or is frivolous or vexatious.

2 In 2019, the FSCA reported that it had investigated 421 cases, taken enforcement action in 91 cases and imposed approximately 138 million rand in penalties since 1999. This includes investigations by its predecessor. See 'FSCA Press Release: Report by the FSCA on status of various investigations', dated 4 March 2019, available at: www.fsca.co.za/News%20Documents/FSCA%20Market%20Abuse%20Investigations%20Press%20Release%20-%2004%20March%202019.pdf.

Any two shareholders of a company may propose that a resolution concerning any matter in respect of which they are each entitled to exercise voting rights (e.g., the removal of a director) be submitted to shareholders for consideration at the next shareholders' meeting, at a meeting demanded by shareholders or by written vote.[3]

Corporate actions that require shareholder approval present opportunities for shareholder intervention. Generally, ordinary resolutions may be passed by a majority of more than 50 per cent, and special resolutions with a majority of at least 75 per cent, of the voting rights exercised on the resolution. Blocs of shareholders may therefore cooperate to block or pass resolutions. In particular, a minority shareholder or shareholders holding 25 per cent of the voting rights may block special resolutions (e.g., to approve a buy-back, an issue of securities or a fundamental transaction).

In certain instances, the Companies Act and the Listings Requirements impose special approval requirements. For example, resolutions proposing fundamental transactions (statutory mergers, schemes, certain business or asset disposals) require approval at a quorate meeting of 75 per cent of disinterested shareholders present and voting (i.e., excluding voting rights of the acquirer and related or concert parties). Similarly, in respect of JSE-listed companies undertaking related party transactions, the votes of related parties and their associates will not be taken into account in the approval of any resolution in connection with the related party transaction.

ii Access to company records and information

A shareholder can access certain company records to assist with activist proposals and seek the cooperation of other shareholders. Holders of beneficial interests in a company's securities have the right to inspect and copy the company's MOI,[4] securities register, register of directors, reports and minutes of annual meetings, and annual financial statements. If additional information is required for the exercise or protection of a right, a shareholder may be able to rely on the Promotion of Access to Information Act 2 of 2000, enacted to give effect to the constitutional right of access to information.

iii Dissenting shareholders

Dissenting shareholders may frustrate or, in limited circumstances, prevent the implementation of a proposed scheme, merger or sale of all or a greater part of the assets or undertaking. Despite shareholders having approved a special resolution in respect of such a transaction, a company may not implement it without the approval of a court if (1) the resolution was opposed by at least 15 per cent of the voting rights exercised thereon, and any of the dissenting shareholders, within five business days of the vote, requires the company to obtain court approval; or (2) any dissenting shareholder who voted against the resolution, within 10 business days of the vote, successfully applies to a court for a review of the resolution. A court may set aside the resolution only if it is satisfied that the resolution is manifestly unfair to a class of shareholders or the vote was materially tainted by a conflict of interest, inadequate disclosure, a failure to comply with the Companies Act or the company's MOI, or some material procedural irregularity.

3 Shareholders entitled to exercise at least 10 per cent of the voting rights may propose an amendment to a company's memorandum of incorporation (MOI).

4 This is the constitutional document of a company, which is binding among the company, its board and shareholders.

iv Appraisal rights

In certain prescribed circumstances – including schemes, mergers, or sales of all or a greater part of a company's assets or undertaking – a dissenting shareholder may force the company to purchase its shares in cash at a price reflecting the fair value of the shares.[5] This is a 'no fault' appraisal right that enables a shareholder to sell all of its shares and exit the company. It applies if (1) the shareholder notified the company of its objection to the resolution to approve the action or transaction; and (2) the shareholder voted against the resolution (which was nonetheless approved) and complied with procedural requirements to demand that the company buy its shares for fair value.

v Actions and remedies

In extreme cases, a holder of issued securities may apply to court for an order necessary to protect any right of the securities holder, or rectify any harm done to the securities holder by (1) the company due to an act or omission that contravened the Companies Act, the MOI or the securities holder's rights; or (2) any director of the company, to the extent that he or she is or may be liable for a breach of fiduciary duties.[6]

Similarly, a shareholder may apply to court for appropriate relief if any of the following is considered oppressive or unfairly prejudicial, or unfairly disregards the interests of that shareholder:

a the result of any act or omission of the company;

b the manner in which the business of the company is being carried on; or

c the manner in which the powers of a director, prescribed officer or related person are being exercised.[7]

Having considered the application, the court may make any interim or final order it considers fit, including an order restraining the conduct complained of, ordering a compensation payment, or varying or setting aside an agreement or transaction.

The Companies Act also introduced a statutory derivative action that enables a shareholder (among other stakeholders) to demand that the company bring or continue proceedings, or take related steps to protect the legal interests of the company.[8] A company may apply to court to set aside the demand only on the grounds that it is frivolous, vexatious or without merit.

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5 Section 164 of the Companies Act.

6 Section 161 of the Companies Act.

7 Section 163 of the Companies Act.

8 Section 164 of the Companies Act. Section 159 also provides whistle-blower protections for shareholders to make good faith disclosures of information to a relevant regulator where the shareholder reasonably believed at the time of disclosure that the company, director or prescribed officer had: (1) contravened the Companies Act; (2) failed to comply with a statutory obligation; (3) engaged in conduct that endangered or harmed an individual or the environment; (4) unfairly discriminated against a person; or (5) contravened other legislation that could place the company at risk. These shareholders are immune from any civil, criminal or administrative liability, and the relevant shareholder has qualified privilege in relation to the disclosure made, which would encourage shareholder activists seeking to hold the board accountable for its conduct.

vi Stakebuilding

Activists should carefully structure any on-market or off-market stakebuilding, taking into account the legal and regulatory obligations applicable to their particular circumstances.

Disclosure obligations require persons who acquire or dispose of a beneficial interest in securities, such that they hold or no longer hold 5 per cent or any further multiple of 5 per cent of the voting rights attaching to a particular class of securities, to notify the issuer company within three business days of the acquisition.[9] This applies irrespective of whether the acquisition or disposal was made directly, indirectly, individually or in concert with any other person, and options and other interests in securities must be taken into account.

If an acquisition takes the acquirer's beneficial interest in voting rights to 35 per cent or more (whether acting alone or in concert), the acquisition will trigger a mandatory offer to the remaining shareholders, unless a 'whitewash resolution' waiving the mandatory offer is approved by a majority of independent shareholders.

Where a stakebuilding involves two or more persons cooperating for the purposes of proposing an 'affected transaction' or offer, concert party rules in the Companies Act and the Takeover Regulations will apply. The latter also impose strict requirements in relation to dealings in securities before, during and after an offer period.

In addition to disclosure obligations, activists should be mindful of the insider trading offences and the broader framework regulating market abuse under the Financial Markets Act.[10]

vii Defences available to companies and directors' duties

While the Companies Act creates an enabling environment for shareholder activism, it also seeks to 'balance the rights and obligations of shareholders and directors within companies'.[11] As a general principle, it is the board that has primary legal responsibility for managing the business and affairs of the company. In doing so, the directors are subject to various fiduciary duties under the Companies Act and at common law, all of which flow from the overarching duty to act in the best interests of the company at all times. There is no list of factors that a director must consider when assessing what is in the best interests of the company. The Companies Act includes a statutory US-style business judgement rule, which affords directors some latitude and a degree of protection in responding to shareholder activism.

There are various defences available to boards and companies when faced with shareholder activism. Companies that have anticipated and prepared for activism, and carried out strategic stakeholder engagements, will be better placed to respond decisively and quickly to activist campaigns that may not be in the best interests of the company. In assessing an appropriate response to shareholder activism, a board needs to have regard to the interests of the company and its stakeholders writ large. In doing so, it will have to consider the short-, medium- and long-term interests of the company.

In a transactional context, the Companies Act contains a 'no frustrating action' rule that requires the board to refrain from taking any action vis-à-vis the company that is directed at frustrating an offer, or which could effectively result in a bona fide offer being frustrated, or shareholders being denied an opportunity to decide on its merits.[12]

9 The issuer then has 48 hours to disclose the acquisition to the market and shareholders.

10 See Chapter X of the Financial Markets Act.

11 Section 7 of the Companies Act, which sets out the purposes of the Companies Act.

12 Section 126 of the Companies Act.

III KEY TRENDS IN SHAREHOLDER ACTIVISM

i Profile of activist investors

In broad terms, it is possible to distinguish between economic activists and governance activists. Economic activists in South Africa primarily comprise institutional investors (such as asset managers, collective investment schemes, hedge funds, insurers, retirement and pension funds) whose activism is often event-driven and is generally directed at extracting greater shareholder value. Governance activists typically seek to influence board composition and company policy, and to improve corporate governance.

Non-profits and NGOs, such as Just Share, the Raith Foundation and the Centre for Environmental Rights, have actively pursued ESG-related agendas.

A number of prominent individual activists also regularly challenge companies on corporate governance, ESG and related issues.

Many institutional investors regard shareholder activism as integral to their investment strategies and will pursue both economic and governance activism. Examples of investors who have pursued both economic and governance activism include Allan Gray, Value Capital Partners and Foord Asset Management. The Public Investment Corporation (PIC), an investment management company owned by the South African government, which manages the assets of the Government Employees Pension Fund and other social security funds, holds significant stakes in a number of JSE-listed companies and exercises considerable influence as a shareholder, particularly in M&A contexts.

ii Companies targeted by activist investors

Activism in South Africa has not been restricted to any particular sectors, or by company size or performance. There are many endogenous and exogenous factors that might render a company a more vulnerable target of an activist campaign.

iii Activist campaigns

The objectives of activists vary, and activists will use different tactics and strategies in pursuit of their objectives. Shareholder engagement is more often than not private, 'behind closed doors', but may play out in public.[13] Institutional investors are often very influential, particularly when acting collaboratively.

Historically, most campaigns in South Africa have focused on executive compensation and board composition.

On remuneration, following the introduction of 'say-on-pay' rules, certain JSE-listed companies have had to reconsider their remuneration policies following significant shareholder opposition to such policies or implementation reports.[14]

13 See Mans-Kemp, N. & Van Zyl, M., 2021, 'Reflecting on the changing landscape of shareholder activism in South Africa', *South African Journal of Economic and Management Sciences* 24(1), a3711. https:// doi. org/10.4102/sajems. v24i1.3711 (accessed 25 June 2021).

14 In particular, the King Code contains recommendations relating to executive remuneration, including a recommendation that companies should produce and disclose, in respect of a reporting period, a remuneration policy and a report on the implementation of that policy. This remuneration policy and implementation report must be tabled annually for a separate non-binding advisory vote by shareholders at the company's annual general meeting (AGM). If 25 per cent or more voting rights are exercised against any part of this remuneration policy, the board must engage with shareholders in good faith to understand shareholder dissatisfaction and the reasons for dissenting votes. The board is required to appropriately

Regarding board composition, campaigns have forced companies to take steps to change the make-up of their boards or pushed for the resignation of the CEO. A noteworthy example of this was in 2014, when activists sought to remove the entire board of PPC, a cement manufacturer.[15]

Recent campaigns by Just Share, among others, have sought to have resolutions tabled at listed company AGMs that, if passed, would require the companies (particularly in the banking sector) to disclose or report to shareholders on climate risk, plans to address climate-related transition risks, assessments of greenhouse gas emissions in financing portfolios and policies on lending to carbon-intensive activities and projects.

In the M&A context, we have seen shareholders using their influence to try to block or force M&A activity. Recent examples of the former include shareholder opposition to a proposed takeover of PPC,[16] and Prudential's opposition to an attempted takeover of poultry producer Sovereign Foods by Country Bird Holdings.[17] An example of the latter is Grand Parade Investment's (GPI) disposal of its interests in certain franchises (described in Section IV).

Recent campaigns, for example that against La Concorde (described in Section IV), also demonstrate the potential for shareholders, in certain statutorily prescribed circumstances, to delay potential M&A transactions by requiring a company to obtain court approval before implementation or to exit their investments for fair value by exercising their appraisal rights.

iv Outcomes and the path to resolution

Recent campaigns relating to climate-related matters, particularly in the banking sector, demonstrate that activists can use a variety of different approaches to pursue the same ends, with varying degrees of success and a range of possible outcomes. Outcomes also depend to a large extent on the approach adopted by the company that is the target of an activist campaign: responses vary from summary dismissal to collaborative engagement, to active opposition.

As noted above, shareholder activists who hold even nominal stakes in companies are afforded relatively strong rights and protections. Companies should focus on good corporate governance and proactively participate in appropriate levels of shareholder engagement, with particular focus on creating and unlocking shareholder value. This includes abiding by the disclosure and engagement recommendations of the King Code, particularly in the context of listed companies.

address reasonable and legitimate concerns raised in the evaluation of performance. Although the advisory vote given to shareholders is non-binding, this vote coupled with increased disclosure enables greater shareholder activism in that it encourages the board to engage with shareholders, promotes transparency and provides shareholders with a platform to express their dissatisfaction.

15 During 2014, a group of shareholders requisitioned a special shareholders' meeting to consider the removal of the entire board of PPC and to replace it with the nominees of the requisitioning shareholders. These measures successfully forced the board to engage with the requisitioning shareholders' concerns.

16 In 2018, PPC was the subject of a merger attempt by a consortium comprising its smaller rival AfriSam and a Canadian investment house, Fairfax Financial Holdings. This failed as a result of shareholder resistance to a perceived undervaluation of PPC. Following failure of the proposed transaction, activist shareholders pressed for the removal of the chairperson and reconstitution of the PPC board.

17 Chris Wood 'Shareholder activism (2): Sovereign Foods: Defending against a hostile takeover', August 2018, available at: https://prudential.co.za/insights/articlesreleases/shareholder-activism-2-sovereign--foods-defending-against-a-hostile-takeover.

In preparing for increased shareholder activism in South Africa, companies should continually and carefully monitor their shareholder portfolios for activists, assess potential vulnerabilities, and anticipate and prepare for campaigns on a case-by-case basis. Boards and companies that can demonstrate value creation over time and adherence to principles of good governance, including careful stakeholder engagement and responsible corporate citizenship, are less likely to find themselves vulnerable to activism. They are also more likely to have anticipated and planned for activism, and to be able to successfully communicate a well-articulated, carefully prepared and strategic response to particular instances of activism.

IV RECENT SHAREHOLDER ACTIVISM CAMPAIGNS

i Capital Appreciation

In June 2022, the Supreme Court of Appeal (SCA) held that a repurchase by a company of 5 per cent or more of its issued shares triggers the appraisal rights. In July 2019, Capital Appreciation completed a specific repurchase of shares in excess of the 5 per cent threshold in Section 48(8) of the Companies Act. Dissenting minority shareholders objected to the special resolution required to approve the share repurchase and exercised their appraisal rights in Section 164 of the Companies Act (described in Section II, above) to require Capital Appreciation to purchase their shares for fair value. Capital Appreciation made an offer of 0.8 rand per share to the dissenting shareholders, which the latter rejected. When the dissenting shareholders applied to the High Court for an order to determine the fair value of the shares, Capital Appreciation contended that they were not entitled to the appraisal rights. Capital Appreciation lost in the High Court and appealed to the SCA, which dismissed the appeal. The SCA essentially held that a share repurchase that is subject to Section 48(8) is a fundamental transaction that is subject to the requirements of Section 114 and Section 115, which makes provision for dissenting shareholders to enjoy the benefit of an appraisal right: the 'right of dissenting shareholders, who do not approve of certain triggering events, to opt out of the company by withdrawing the fair value of their shares in cash'.[18]

The Companies Amendment Bill 2021 proposes to delete Section 48(8) and replace it with a new section that does not refer to Sections 114 and 115, and therefore does not trigger any appraisal rights.

ii GPI

In November 2018, GPI, a franchisee of Burger King, Dunkin' Donuts and Baskin-Robbins, was the subject of activism by a consortium of disgruntled minority shareholders.[19] The consortium requisitioned an extraordinary general meeting (EGM) to overhaul the board and appoint four of its own non-executive directors. It sent a letter to GPI detailing its grievances: doubts about the competency, skills and independence of the board; large bonuses paid to executive directors despite a collapsing share price and dwindling dividend;

18 *Capital Appreciation Ltd v. First National Nominees (Pty) Ltd and Others* (280 of 2021) [2022] ZASCA 85 (08 June 2022), available online at: https://lawlibrary.org.za/za/judgment/supreme-court-appeal-south-africa/2022/85 (accessed 15 June 2022).

19 The consortium comprised Kagiso Asset Management, Denker Capital, Excelsia Capital, Westbrooke Alternative Asset Management and Rozendal Partners.

poor capital allocation decisions; and an exodus of key executives. After GPI failed to abide by a JSE directive ordering it to notify investors of the letter, the JSE issued the letter to shareholders directly.

An investor presentation preceded the EGM, during which GPI's interim CEO threatened 'war' against the activists, branding them 'short-termists' and 'usurpers'. At the EGM, the consortium gained sufficient shareholder support to appoint two of its preferred nominees to the board as non-executive directors. Days later, the CEO resigned, shortly before a vote on her appointment at the company's AGM, and shortly after Value Capital Partners, a turnaround specialist, acquired an influential stake in GPI.

In February 2019, GPI announced that it was exiting its interests in the Dunkin' Donuts and Baskin-Robbins franchises. The consortium had long pushed for GPI to exit the chains, given their track record of underperformance – since their launch in 2016, the South African outlets struggled to gain traction, incurring cumulative losses of over 96 million rand.[20]

iii La Concorde

In June 2018, the High Court considered the issue of whether a dissenting shareholder in a holding company is entitled to exercise appraisal rights (mentioned above) in respect of a subsidiary's disposal of all or the greater part of its assets or undertaking.[21] Individual activist Albie Cilliers exercised his appraisal rights in respect of a sale of assets by a wholly owned subsidiary of La Concorde. After rejecting La Concorde's initial offer of 13.47 rand per share, Cilliers applied to court for a declaration that the valuation did not represent fair value. La Concorde countered by challenging Cillier's entitlement to appraisal rights at all, arguing that Section 164 of the Companies Act granted such rights to shareholders of the disposing company only (i.e., the subsidiary, not the holding company).[22]

Notwithstanding that Cilliers did not hold shares in the subsidiary that was disposing of the assets, the High Court found in his favour, adopting a purposive approach to the appraisal right. The Court held that the appraisal right was introduced to protect minority shareholders, particularly where they are unable to effectively influence company direction or pursue private actions. To treat dissenting shareholders in a holding company any differently from those in a subsidiary, the Court reasoned, would undermine the objective of protecting minority shareholders. Correctly interpreted, the relevant provisions of the Companies Act

20 *Business Insider*, 29 November 2018, Helena Wasserman, 'Amid a war over Burger King's South African owner, this investor says Dunkin' Donuts and Baskin-Robbins should be shut down', available at: www.businessinsider.co.za/war-over-burger-king-may-claim-dunkin-donuts-2018-11; *Business Day*, 18 October 2018, Marc Hasenfuss, 'Hell hath no fury like Grand Parade's Hassen Adams', available at: www.businesslive.co.za/fm/money-and-investing/2018-10-18-hell-hath-no-fury-like-grand-parades-hassen-adams; *Business Day*, 13 December 2018, Marc Hasenfuss, 'A revolving door of CEOs at Grand Parade', available at: www.businesslive.co.za/fm/fm-fox/2018-12-13-a-grand-parade-of-revolving-ceos; *Business Day*, 18 February 2019, Larry Claasen, 'Activist investors win as GPI closes Dunkin' Donuts and Baskin-Robbins in SA', available at: www.businesslive.co.za/bd/companies/retail-and-consumer/2019-02-18-activist-investors-win-as-gpi-closes-dunkin-donuts-and-baskin-robbins-in-sa.

21 See *Cilliers v. La Concorde Holdings Ltd and Others* 2018 (6) SA 97 (WCC).

22 *Business Day*, 19 June 2017, Ann Crotty, 'Albie Cilliers steps up battle over KWV shares amid Vasari sale', available at: www.businesslive.co.za/bd/companies/retail-and-consumer/2017-06-19-albie-cilliers-steps-up-battle-over-kwv-shares-amid-vasari-sale.

gave appraisal rights to both sets of shareholders. Therefore, Cilliers, as a minority shareholder in the La Concorde holding company, was capable of exercising a shareholder appraisal right in relation to the subsidiary's disposal of assets.

iv Steinhoff class action

The *Steinhoff* judgment dealt with the first shareholder class action brought for certification before the South African courts.[23] Following the collapse of Steinhoff's share price in late December 2017, a retired pensioner sought authorisation to represent shareholders in a class action to hold, among others, certain Steinhoff companies and their directors liable for breaches of statutory and common law duties of care.

The shareholders alleged that the companies, through their directors, had engaged in unlawful transactions, the effect of which was to overstate their assets, income and profits, understate their liabilities, and render their financial statements non-compliant with prescribed reporting standards. They sought to hold the companies and directors liable: (1) at common law, in delict or tort, for losses caused to shareholders for negligent misstatements in the financial statements; and (2) under the Companies Act, on the basis that contraventions of statutory duty by the companies and their directors caused loss to shareholders, and gave rise to liability in terms of Section 218(2) or Section 20(6) of the Companies Act for the damage suffered by shareholders.[24]

Common law claim

For the shareholders to have a claim in delict wrongfulness had to be established. Negligent misstatements that cause pure economic loss are a category of case where wrongfulness is recognised if the plaintiff can demonstrate that a legally recognised right or interest has been infringed.[25] In considering whether the shareholders have a legally recognised right or interest that had been infringed by the Steinhoff companies and its directors, the court looked to fundamental principles of company law.

It is a fundamental principle of South African company law that, in general, directors owe fiduciary duties to the company and not to its shareholders.[26] While it is possible that directors may owe (additional) fiduciary duties to shareholders in special circumstances, namely where there is some special relationship subsisting between the directors and the

23 *Dorothea De Bruyn v. Steinhoff International Holdings N.V. and 41 others* (29290/2018) [2020] ZAGPJHC 145 (26 June 2020) (not yet reported), available online at: http://www.saflii.org/za/cases/ZAGPJHC/2020/145.html.

24 The companies and directors were alleged to have breached Sections 22 (prohibition against reckless trading), 28 (accounting records), 29 (financial statements), 30 (annual financial statements), 40 (consideration for shares) and 76 (standards of directors' conduct) of the Companies Act.

25 The Constitutional Court has explained the general principle of the law of delict/tort that conduct causing pure economic loss is not prima facie wrongful, and that wrongfulness must be positively established. Broadly speaking, the wrongfulness enquiry looks into whether it is reasonable to recognise conduct as wrongful and therefore attracting liability, based on policy and the legal convictions of the community.

26 This is entailed by: (1) the *Salomon* principle that a company is distinct from its members/shareholders; and (2) the rule in *Foss v. Harbottle*, which requires that the company and not its shareholders have an action for wrongs done to the company and losses suffered by the company. Both principles stem from the United Kingdom and are principles are reflected in South African common law and certain provisions of the Companies Act, in particular Sections 19 (legal status of companies), 76 (standards of directors' conduct) and 77 (liability of directors).

shareholders,[27] there is no general fiduciary duty owed by directors to shareholders of a company. The court found that there was no basis on the shareholders' case to find that the Steinhoff directors or the companies, by virtue of some special relationship, owed any fiduciary duties or duty of care to the shareholders. Therefore, the shareholders lacked a cause of action because, absent a finding of wrongfulness, there could be no delict.

Statutory claims

Section 218(2) of the Companies Act provides that: 'Any person who contravenes any provision of th[e Companies] Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention.' The court held that: (1) Section 218(2) should not be interpreted literally, as that would lead to incurable contradictions when considered in the light of the other provisions of the Companies Act;[28] and (2) what Section 218(2) does is recognise that loss or damage may arise from contraventions of the Companies Act and confer a right of action. Questions concerning who enjoys the right of action, what the right consists of, and against whom the right may be exercised, must be resolved by reference to the substantive provisions of the Companies Act implicated by the particular contravention – bearing in mind that the Companies Act attaches different regimes of liability to different contraventions.[29]

Section 20(6) of the Companies Act provides that: 'Each shareholder of a company has a claim for damages against any person who intentionally, fraudulently or due to gross negligence causes the company to do anything inconsistent with: (a) th[e Companies] Act; or (b) a limitation, restriction or qualification contemplated in this section [20], unless that action has been ratified by the shareholders in terms of subsection (2).'

27 *Peskin v. Anderson* [2001] 1 BCLC 372 at [30]–[37].

28 For example, Section 77(2)(a) provides that a director may be held liable in accordance with the principles of common law for breaches of fiduciary duty for losses, damages or costs sustained by the company as a result of breaches of duties in Sections 75, 76(2) or 76(3)(a) or (b) of the Companies Act. Such duties are owed to the company and at common law, as noted above, directors may be liable to the company but not the shareholders for directors' breaches of those duties – even if the shareholders suffered a loss as a result of the breaches. Moreover, at common law the *Prudential* principle of 'reflective loss' provides that a shareholder cannot sue for the diminution in value of his or her shares where the loss is simply a reflection of the loss suffered by the company. (See *Prudential Assurance Co Ltd v. Newman Industries Ltd* (No. 2) [1982] 1 Ch 204 (CA), referred to at paragraph 186 of the *Steinhoff* judgment.) If interpreted literally, Section 218(2) would be read to impose liability on a director who contravened a duty in Section 76(3) in favour of shareholders, whereas the liability regime established and regulated by Section 77(2) imposes no such liability. Additionally, the literal interpretation was problematic in that it would give rise to wholesale liability, and an undifferentiated conception of permissible plaintiffs, without the regulating concepts of fault, foreseeability and remoteness.

29 *Steinhoff*, at paragraphs 187–193 and 213. See also *Hlumisa Investment Holdings (RF) Ltd and Another v. Kirkinis and Others* (Case No. 1423/2018) [2020] ZASCA 83 (3 July 2020), in which the Supreme Court of Appeal considered whether Section 218(2) enabled a claim by a shareholder in relation to the diminution of value of shares in African Bank due to various alleged breaches of the Companies Act by the company's directors. The SCA held that the company was the proper plaintiff for breaches by directors of duties owed to the company, and that the rule precluding shareholders from claiming for reflective loss had not been abolished by Section 218(2) of the Companies Act.

Section 20(6) does not specify whether a shareholder has a claim for damage suffered by the shareholders or the company. Having regard to Section 20 as a whole,[30] the court held that Section 20(6) imposes liability on persons who cause loss to the company, and requires those who have caused the company to act ultra vires or unlawfully to make good to the company (by way of damages) the loss they have caused to the company. It does not give rise to liability for the damage that shareholders may have suffered by reason of the unlawful or ultra vires actions of the Steinhoff companies. The company may be compensated for its loss at the instance of the shareholders, which would indirectly benefit the shareholders.

In weighing the various factors that are to be considered in an application for certification,[31] Unterhalter J ultimately held that, as a matter of law, the class action failed to raise a triable issue: as pleaded it did not disclose a cause of action. Therefore, whatever the virtues of the class action, certification could not be granted: 'to trigger the machinery of a class action to determine something that does not exist in law . . . would be to place a ghost in the machinery of justice'.[32]

V REGULATORY DEVELOPMENTS

The fourth iteration of the King Code (King IV) adopts a qualitative, outcomes-based 'apply and explain' application and disclosure regime, in contrast with earlier iterations that imposed an 'apply or explain' regime. The King Code promotes a stakeholder-inclusive approach to corporate governance (as opposed to a shareholder-centric approach), which regards shareholders as an important subset of stakeholders who, by virtue of their rights as shareholders, are able to hold companies and their boards to account. The King Code, therefore,

30 Section 20 is broadly concerned with the validity of company actions. It recognises that persons may cause a company to act beyond its powers or some other limitation in its constitutional documents, and/or unlawfully in contravention of the Companies Act and sets out various remedial options available to shareholders and other constituencies (including directors and prescribed officers) in those circumstances. Section 20(6) confers a right of action for damages on each shareholder of a company against a person who, intentionally, fraudulently or through gross negligence, caused the company to do anything inconsistent with either the Companies Act or a limitation on the purposes, powers or activities of the company in its constitutional documents (the latter, ultra vires actions).

31 In *Children's Resource Centre Trust v. Pioneer Food (Pty) Ltd* 2013 (2) SA 213 (SCA) at paragraph 26, the Supreme Court of Appeal set out factors that should be weighed in deciding whether to certify a class action: the existence of a class identifiable by reference to objective criteria; the proposed class representative is suitable to conduct the action and represent the class; a cause of action raising a triable issue; the right to relief requires the determination of issues of fact or law, or both, common to all members of the class; the relief sought or damages claimed flow from the cause of action and are ascertainable and capable of determination; where damages are claimed, there is a procedure by which to allocate the damages to members of the class given the composition of the class and the nature of the proposed action; and that a class action is the most appropriate means by which the claims of the class may be determined. In *Mukaddam v. Pioneer Foods (Pty) Ltd* 2013 (5) SA 89 (CC) at paragraphs 34–40, the Constitutional Court held that the above factors are not prerequisites for certification but are considerations to be weighed under the overarching principle of what is required by the interests of justice. And as Unterhalter J put it in *Steinhoff*, at paragraph 25: '[F]actors relevant to certification may weigh in different ways. Certain factors may weigh with the certification court to incline the decision one way or another. Other factors may be so weighty that the scales tip decisively. Every factor is to be weighed, and none displaces the ultimate exercise of weighing all in the balance to determine where the interests of justice lie. But that does not mean that a factor in a particular case may weigh so heavily that it points clearly to what the interests of justice require.'

32 *Steinhoff*, at paragraphs 299–300.

encourages active shareholder engagement through a number of its recommendations.[33] As such, it creates an opportunity for a framework for the responsibilities of shareholders, particularly institutional investors, to be incorporated in the corporate governance system of checks and balances.

In June 2019, the FSCA published Guidance Notice 1 of 2019 for pension funds on Regulation 28 of the Pension Funds Act 24 of 1956. The latter imposes a legal obligation on pension funds to, before making an investment in and while invested in an asset, consider any factor that may materially affect the sustainable long-term performance of the asset, including ESG factors. The Guidance Notice recommends 'active ownership' by pension funds, being the prudent fulfilment of responsibilities relating to the ownership of, or an interest in, an asset. These responsibilities include guidelines to be applied for the identification of sustainability concerns in that asset, and mechanisms of intervention and engagement with the responsible persons in respect of the asset when concerns have been identified.

A revised draft Code for Responsible Investment in South Africa (CRISA 2.0) was published for public comment in 2020.[34] CRISA is a voluntary Code aimed at providing guidance to institutional investors on the execution of investment analysis and investment activities, and the exercise of rights so as to promote sound governance. To that end, CRISA 2.0 sets out various principles and practice recommendations with a clear emphasis on ESG and broader sustainable development issues. It also proposes a shift in application regime from 'apply or explain' to an outcomes-based, 'apply and explain' regime.

Principle 1 of CRISA 2.0 contemplates integration of sustainable finance: 'Investment arrangements and activities reflect a systematic approach to integration of sustainable finance practices, including the identification and consideration of materially relevant ESG and broader sustainable development considerations.' Principle 2 places a greater emphasis on the diligent discharge of stewardship activities: 'Investment arrangements and activities demonstrate the acceptance of ownership responsibilities (where applicable) and enable diligent discharge of stewardship duties through purposeful engagement and voting.' Among its recommendations is that 'investment arrangements and activities should incorporate mechanisms that support the diligent discharging of stewardship duties generally and particularly as it relates to ESG and broader sustainable development concerns'. These mechanisms include:

a assessing the extent and quality of disclosure by investee organisations or issuers (as the case may be), including evaluating integrated reporting as a reflection of value being created, preserved or destroyed;

33 Among other things, the King Code recommends that the board encourage shareholders to attend general meetings and engage with shareholders through various means such as websites, advertising and press releases. Certain parts of the King Code have been incorporated into legislation by reference. The King Code has recently been updated to introduce greater disclosure recommendations, including in respect of board committees (e.g., remuneration committees) and CEOs (e.g., in respect of notice periods, contractual conditions relating to termination and succession planning).

34 CRISA 2020 Revision Consultation Draft, November 2020, available online at: https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/1D7CF73B-B95B-453F-A8E3-D19829D18FBD/CRISA_2.0_Draft_for_public_comment.November2020__00000004_.pdf (accessed 27 June 2021). The draft revised CRISA Code is published by the CRISA Committee for comment and does not constitute a final document. The CRISA Code of 2011 remains in place until such time as a revised Code has been finalised and an effective date determined and published. Also see National Treasury's Draft Technical Paper on Financing a Sustainable Economy, May 2020, available online at: http://www.treasury.gov.za/publications/other/Sustainability%20technical%20paper%202020.pdf.

b approaches to intervention and engagement when concerns have been identified, and the means of escalation when concerns cannot be resolved; and

c criteria for voting decisions, participation in AGMs or use of proxies or voting instructions, and for public disclosure of voting records.

The Companies Amendment Bill 2021 proposes changes to remuneration reporting and approval requirements for public and stat-owned companies, which are designed to strengthen shareholder and stakeholder oversight of pay. The Bill contemplates a remuneration report that must comply with the prescribed format and content requirements and include a policy on remuneration of directors and prescribed officers. Notably, companies will be required to publish details of their highest paid employee, their lowest paid employee, their average remuneration, their median remuneration and the gap between the top 5 per cent highest paid and the bottom 5 per cent lowest paid employees.

The remuneration report must be approved by the board and approved by shareholders every year at the AGM by way of ordinary resolution. If the remuneration report is not approved, the remuneration committee must, at the next AGM, present on how shareholder concerns have been addressed and the non-executive directors that serve on the committee are required to stand down for re-election every year of such rejection.

The remuneration policy need only be approved every three years or where there are material changes. If the remuneration policy is not approved, special meetings may be called until it is approved. No changes may be implemented until approved.

VI OUTLOOK

Recent high-profile corporate scandals and governance failures have resulted in calls for increased shareholder oversight of boards and investee companies in South Africa. Shareholder demands for greater levels of accountability, transparency and return on investment are on the rise. A failure to engage with sophisticated activist shareholders, or provide them with the levels of transparency demanded, may leave the board exposed to shareholder disapproval sparked by shareholder activists who are armed with an increased amount of information and a variety of regulatory rights and protections.

Shareholders are becoming increasingly active on such matters as diversity, board composition, performance and tenure, executive remuneration policies, transparency and ESG issues. This is being driven in part by increasing civic action on high levels of inequality, climate change, ongoing debates about corporate purpose and enhanced reporting and disclosure requirements. A noteworthy development on the disclosure front is the JSE's publication, on 14 June 2022, of its Sustainability Disclosure Guidance and Climate Disclosure Guidance.[35] This is voluntary guidance for JSE-listed companies on sustainability and climate-related disclosure that draws on existing international frameworks while providing for South African context. Enhanced corporate disclosures on these and other issues are likely to provide shareholder activists with a new material to use in their campaigns, and the ability to compare and assess companies' performance over time.

Issues relating to ESG and sustainability are the focus of many recent campaigns and will remain high on the agenda. We expect local and international institutional investors,

35 Available online at: https://www.jse.co.za/our-business/sustainability/jses-sustainability-and-climat e-disclosure-guidance (accessed 15 June 2022).

in particular pension funds, mutual funds and insurers, to play an increasingly active and pivotal role in influencing corporate strategy and M&A with reference to sustainability and ESG factors. Careful consideration of these issues has become essential to corporate strategy and governance. Companies that pay inadequate attention to these issues are increasingly likely to become exposed to business, credit, market, reputational, legal and other risks, which could have a material adverse effect on their businesses over the medium- to long-term.

Appendix 1

ABOUT THE AUTHORS

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Ezra Davids is chairman and senior partner of Bowmans, and specialises in M&A, capital markets and securities law. Ezra is a member of the governing Council of the University of Cape Town. He sits on the board of trustees of the Legal Resources Trust (a non-profit human rights organisation using the law as an instrument of justice); is a director of Freedom Under Law (a non-profit organisation dedicated to the promotion of the rule of law in Southern Africa); and is a patron of the Student Sponsorship Programme (a non-profit organisation that enables academically talented, low-income students to excel in South Africa's best high schools). He is also the former chairman of the Recent Developments in M&A Subcommittee of the Corporate and M&A Committee of the International Bar Association and is a regular contributor to international M&A and ECM publications. Ezra was recently named by the New York-based Global M&A Network as one of the Top 50 Global M&A Dealmakers, and as South African Lawyer of the Year at the Chambers Africa Awards 2022. Ezra is the first practising African lawyer to be featured on the cover of *The American Lawyer*.

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Ryan Kitcat is a partner in the corporate/M&A practice area at Bowmans. Ryan specialises in public and private M&A and general corporate and commercial law. He has advised JSE-listed and multinational clients on a variety of national and cross-border mandates. He has worked in particular in the energy and natural resources, education, mining, hospitality, private security and telecommunications sectors. His expertise extends to B-BBEE transactions, corporate reorganisations, corporate governance, shareholder activism and takeovers. He is a regular contributor to international M&A publications. In 2018, Ryan spent time in the London office of Freshfields Bruckhaus Deringer on a *StrongerTogether* secondment. In 2019, Ryan completed the course Impact Investing in Africa through the University of Cape Town Graduate School of Business.

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