Unpacking the amendments of the Companies Act

An in-depth analysis

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THE COMPANIES AMENDMENT ACT NO 16 OF 2024

In September 2018, a draft Companies Amendment Bill was published in the Government Gazette for public comment. This was followed by the publication on 1 October 2021 of a second version of the Bill, also for public comment. During this 3 year period and thereafter, there was substantial discussion with business and labour represented at NEDLAC, the National Economic Development and Labour Council.

The Department of Trade, Industry and Competition ("DTIC") stated in its comments on the Bill that the series of amendments in the Bill are aimed at achieving three policy objectives, namely:

1. improving ease of doing business in respect of certain provisions of the Companies Act;

2. providing for greater transparency on wage ratios; and

3. addressing true or beneficial ownership of companies in order to address money laundering challenges.

This process was changed in 2022 for the following reason: There is a global organisation called The Financial Action Task Force ("FATC"), which was formed in 1949 in order to combat money laundering and terrorist financing. FATC makes so-called FATC recommendations and then assesses whether a country meets these recommendations. Countries that don't meet the FATC assessment standards to a certain degree may be put on the FATC blacklist or greylist. Only Iran and North Korea are on the blacklist. The greylist comprises a number of jurisdictions such as Panama, Bahamas, Pakistan and South Africa. FATC continually monitors progress in implementing its recommendations through peer reviews of member countries. South Africa has been a member of FATC since 2003. FATC assessed South Africa's AML/TF system in 2019 and produced an Evaluation Report. The report concluded that South Africa has a solid legal framework for combating money laundering and terrorist financing but significant shortcomings remain. In particular, the country needs to pursue money laundering and terrorist financing in line with its risk profile, including by proactively seeking international cooperation, detecting and seizing illicit cash flows, <u>and improving the availability of beneficial ownership information</u>. Authorities need to make better use of the financial intelligence products provided by South Africa's financial intelligence unit. The

assessment was led by the International Monetary Fund. As far as transparency and beneficial ownership of legal persons, as well as transparency and beneficial ownership of legal arrangements are concerned, South Africa was found to be "partially compliant". South Africa then decided to immediately strengthen its beneficial ownership legislation. This manifested itself in the promulgation in 2022 of the General laws (Anti Money-Laundering and Combatting Terrorist Funding) Amendment Act of 2022, which came into effect on 1 April 2023. The Act amends 4 pieces of legislation, being the Companies Act, the FICA Act, the Trust Property Control Act and the Financial Sector Regulation Act. This Act served one purpose – to improve the disclosure and availability of beneficial ownership information.

In the result, the third of the 3 aforementioned policy objectives of the DTIC, namely addressing true or beneficial ownership of companies to address money laundering challenges, was accomplished via this General Laws Amendment Act, and is not dealt with in the 2024 Companies Amendment Act.

The DTIC stated that the Amendment Act addresses proposed amendments to the Companies Act to cover the following significant subjects, apart from some technical amendments:

1. to provide for the preparation, presentation and voting on a company's remuneration policy and a directors' remuneration implementation report;

2. to provide for the filing of a company's annual financial statements, the company's securities register and a copy of the register of disclosure of beneficial ownership with CIPC;

3. to differentiate where the right to gain access to companies' records may be limited;

4. to clarify when a Notice of Amendment of a Memorandum of Incorporation (MOI) takes effect;

5. to empower the court to validate the irregular creation, allotment or issue of shares;

6. to exclude subsidiary companies from certain of the requirements relating to inter-group financial assistance;

7. to provide for instances where a special resolution is required for the acquisition of its own shares by a company;

8. to provide for the circumstances under which a private company will fall within the ambit of the takeover provisions of the Act;

9. to deal with the composition of the social and ethics committee and the publication of an application for exemption from the requirement to appoint a social and ethics committee;

10. to provide for the presentation and approval of the social and ethics committee report at the annual general meeting or other meetings of shareholders; and

11. to provide for matters connected with the above.

The Companies Amendment Act, 2024 was finally gazetted on 30 July 2024. However, notice of the date when it will come into operation has yet to be gazetted.

BENEFICIAL OWNERSHIP OF SECURITIES

The Companies Act currently recognizes (and has always recognized) the principle that a security may be registered in the name of a person who acts as the agent or "nominee" of the "true" or "real" owner of that security. It is a long-standing and ubiquitous business practise, especially among banks and other financial institutions, to register securities in the names of nominees. Although the use of nominee companies has been abused in a number of instances, there are many cogent, legitimate and credible reasons why a person would wish to hold his securities in the name of a nominee.

Legislation which came into effect on 1 April 2023 now compels disclosure of the "real" or "true" direct or indirect ultimate owner or effective controller of 5% or more of the securities in all companies. Government's aim in enacting the new legislation is to assist law enforcers in combatting money laundering, terrorist financing, tax evasion and corruption. As stated above, this new legislation takes the form of the General Laws (Anti-Money Laundering and Combatting Terrorist Financing) Amendment Act No 22 of 2022, sections 55 to 61 of which amend the Act in various respects, as well as in the form of regulations pursuant to these new sections.

The new sections of the Act require public companies and large private companies to establish and maintain a register of disclosures of beneficial interests as well as a register of persons

who hold beneficial interest equal to or in excess of 5% of the total number of securities of that class issued by the company, together with the extent of those beneficial interests. As far as most private companies are concerned, the Act requires them to keep records of the names and certain details of the so-called “beneficial owners” of more than 5% of their securities, to compel such private companies to then furnish this information to CIPC and to enable what CIPC terms “law enforcement and Competent authorities” to gain access to this information from CIPC. This manner in which Government has attempted to achieve these aims are described below.

The cornerstone provision for private companies is the new section 50(3A) of the Act, which provides that a private company “must record in its securities register prescribed information regarding the natural persons who are the beneficial owners of the company, in the prescribed form, and must ensure that this information is updated within the prescribed period after any changes in beneficial ownership have occurred.”.

The definition of “beneficial owner” is, of course, crucial. **“Beneficial owner”**, in respect of a company, means an individual [i.e. a natural person] ”who, directly or indirectly, ultimately owns that company or exercises effective control of that company.”

In other words, there are two types of beneficial owners, namely a natural person who either, directly or indirectly –

1. ultimately owns that company; or
2. exercises effective control of that company.

Unfortunately, neither the term “effective control” nor the word “control” is defined although some guidance as to the meaning of “control” may be obtained from section 2(2)(a) of the Act, which deals with related and inter-related parties, and section 3(1) of the Act, which deals with holding companies and subsidiaries.

Importantly, this definition then goes on to effectively provide that, in a number of instances, an individual is deemed to ultimately own or effectively control a company by stating that ultimate ownership or effective control includes the following –

“(a) the holding of beneficial interests in the securities of that company;

(b) the exercise of, or control of the exercise of the voting rights associated with securities of that company;

(c) the exercise of, or control of the exercise of the right to appoint or remove members of the board of directors of that company;

(d) the holding of beneficial interests in the securities, or the ability to exercise control, including through a chain of ownership or control, of a holding company of that company;

(e) the ability to exercise control [not ownership], including through a chain of ownership or control, of –

(i) a juristic person other than a holding company of that company;

(ii) a body of persons corporate or unincorporate;

(iii) a person acting on behalf of a partnership;

(iv) a person acting in pursuance of the provisions of a trust agreement; or

(f) the ability to otherwise materially influence the management of that company."

The term "**beneficial interest**" is defined in the Act as meaning, "when used in relation to a company's securities, the right or entitlement of a person, through ownership, agreement, relationship or otherwise, alone or together with another person , to:

(a) receive or participate in any distribution in respect of the company's securities; or

(b) exercise or cause to be exercised, in the ordinary course, any or all of the rights attaching to the company's securities; or

(c) dispose or direct the disposition of the company's securities, or any part of a distribution in respect thereof,

but does not include any interest held by a person in a unit trust or collective investment scheme in terms of the Collective Investment Schemes Act 2002."

The aforesaid two definitions do not conflict with one another. Therefore, both definitions will have to be considered in interpreting the new legislation.

As is logical and therefore expected, the new disclosure requirements have been introduced into those sections of the Act which deal with a company's securities register, being the register of a company's issued securities.

Every company (including a private company) must file an annual return, within thirty business days after each anniversary of its date of incorporation. Failure by a company to do so for two

or more years in succession without satisfactory reasons may result in CIPC deregistering the company. The critical change to the legislation is section 33 of the Act, which has now been amended to require that a company must include in its annual return a copy of its securities register "in such manner and form as prescribed by" CIPC and, in the case of public companies, a copy of its register of disclosure of beneficial interests. Furthermore, CIPC must make the annual return available to any person "as prescribed".

But it does not end there; new section 56(12) provides that a private company must file with CIPC "a record...... in the prescribed form and containing the prescribed information, regarding the individuals who are the beneficial owners of the company, and must ensure that this information is updated by filing notices with the Commission within the prescribed period after any changes in beneficial ownership have occurred".

Regulation 30(10) then states that "[T]he Commission shall provide electronic access to view copies of the documents filed together with an annual return with the Commission .... to such persons and on such conditions as may be determined by the Commission, after consultation with the Minister and the Financial Intelligence Centre." All we know about who "such persons" are at this stage in a CIPC statement that they must be made available to "law enforcement and Competent authorities".

Although the wording of the Regulations is unfortunately unclear, it would appear that –

- the onus of disclosing the beneficial owner or effective controller of a security in a company who holds more than 5% of the company's issued securities will lie on both the securities holder and the company (if it has knowledge of the beneficial owner or effective controller). The securities holder will be obliged to disclose that information to the company even if he is not specifically requested to do so. In the case of a change in beneficial ownership or effective control of more than 5%, such disclosure will have to be made within five business days after the end of the month during which the change occurred;

- the company must update its security register as soon as practical but no later than five business days after such disclosure to reflect the change of information and then file the applicable CoR Form with CIPC within five business days after having done so;

- the following information must be included in the company's securities register in relation to each beneficial owner –

(a) the full name, date of birth, identity number (if South African) or passport number and date of birth (if non-South African);

(b) residential and postal address;

(c) email address if available, unless the person has declined to provide an email address;

(d) confirmation as to the scope of participation in and extent of ownership, or effective control of, the company; and

(e) any other supporting document CIPC may require.

The filing process is fully online and CIPC has issued a booklet entitled "User Guidelines – Beneficial Ownership" for this purpose.

The definition of "beneficial owner" read with that of "beneficial interest" will undergo intense scrutiny by lawyers and other professional advisers to ascertain whether or not it is still possible to avoid disclosure of the "true" or "real" owner or effective controller of more than 5% of the securities in a private company even though the information (theoretically at least) is open to scrutiny only by "law enforcement and Competent authorities". The problem they face is that the wording of the definition of "beneficial owner" is extremely wide; this is due to the use of the words "directly or indirectly", "ultimately", "effective" and, importantly, "includes". The problem is exacerbated by the insertion at the end of the definition of a "catch-all clause", being sub-paragraph (f) thereof, which states that ultimate ownership or effective control "includes the ability to otherwise materially influence the management of that company". In other words, a test of de facto control has been introduced, the satisfaction of which will depend on the facts of the case in question.

The fear, of course, is that somehow or another people other than "law enforcement and Competent authorities" will be able to obtain this information and that the legislature has therefore "thrown the baby out with the bathwater". After all, CIPC administers about 2.1 million active entities. Only time will tell.

SECTIONS 26 AND 30 – ACCESS TO A COMPANY'S RECORDS

New section 30(4)(a) provides that the Annual Financial Statements ("AFS") of each company that is required to have its AFS audited must include particulars showing the "remuneration" (as defined in subsection (6)) and benefits received by each individual director and prescribed

officer, both of whom must be named. This transparency requirement permits stakeholders to see the individual remuneration details of each director.

This is of particular relevance in light of the amendment to Section 26(1), which is to the effect that a person who holds a beneficial interest in any securities issued by a profit company or who is a member of a non-profit company now has the right to inspect and copy the AFS of that company for the 7 years after the date which each such particular statements were issued, as well as the disclosure of beneficial interests in a company.

The amendment to S 26(2) is also new. At present, a private company's AFS are only available to its shareholders, and members of the public can only access the company's securities register. Section 26(2) effectively provides that any person has the right to inspect and copy the MOI and rules (not new), the records of the company's directors (not new), the register of beneficial interests (new), the securities register (not new) and, most importantly, the company's AFS. This right to inspect the AFS does not apply to small private companies, specifically those whose AFS are internally prepared and have a public interest score ("PIS") of less than 100 or whose AFS are independently prepared and have a PIS of less than 350

Where a company receives a request for such inspection or copy, it has 10 days to comply with the request.

The Act also clarifies that, where the disclosure of directors' remuneration must be audited, the company's policy or background statements and its remuneration report need not be audited.

We thus have a new transparency requirement. The right given to any member of the public to inspect the AFS of a private company obviously has major implications for private companies. For example, competitors and contractual counterparties of a private company can now inspect the AFS of their competitors or counterparties. When read with the new Section 30(4)(a), they can also ascertain, for example, the remuneration earned by each executive of a competitor. Surely this infringes on a person's right to privacy? The right to inspect the register of beneficial interests undoubtedly does so. Why should a complete stranger have the right to know how the shareholding in a private company is structured?

This amendment is therefore likely to prove to be controversial since most private companies regard their AFS as being highly confidential, so it would not surprise me if its validity is

challenged in a court of law. As stated, before its amendment, the Act only allowed members of the public to inspect or copy a company's securities register.

SECTION 16 – AMENDMENTS TO THE MOI

Another change to the Act is new section 16(9)(b), which deals with when an amendment to a company's MOI takes effect. Prior to its amendment, Section 16(9)(b) provided that such an amendment take effect on the later of the date on which the Notice of Amendment was filed with CIPC or the date, if any, set out in the Notice of Amendment. This date has practical significance because many transactions require, sometimes as conditions precedent, that an amended MOI must become effective by a certain date, especially given the fact that the MOI in many instances forms an integral part of shareholders agreements in light of the controversial Section 15(7), which effectively provides that the MOI overrides any provision in a shareholders' agreement which is inconsistent with it, and the fact that a company's share structure and the rights attached to its shares now form part of its MOI. The uncertainty was that it was unclear whether the amendment took effect on the date on which the MOI was submitted to CIPC or the date on which CIPC confirmed that the amendment has been accepted by CIPC.

The amendment to Section 16(9)(b) now clarifies the position by stating that an amendment to the MOI takes effect 10 business days after receipt of the Notice of Amendment by CIPC unless it is endorsed or rejected with reasons by CIPC prior to expiry of such 10 business period or such later date, if any, set out in the Notice of Amendment.

This change will affect the timing of transactions since changes to the MOI or a company's share structure can no longer become effective with immediate effect.

Unfortunately, there are still drafting anomalies in the proposed amendment:

2.1 No indication is given as to how one determines the date of receipt by CIPC.

2.2 Presumably, an effective date stipulated in a notice of amendment will also not occur if CIPC rejects the notice in question. The new provision does not provide for this eventuality.

2.3 The meaning of “endorsement” by CIPC is unclear. Presumably, it refers to an acceptance of the filed notice. In such a case, the proposed clause does not state if the amendment is then effective on such earlier date of “endorsement”.

2.4 The proposed clause does not address the timing consequences if CIPC rejects a notice of amendment. Does it mean that a new notice of amendment has to be filed, with another 10 business day waiting period?

So, although the amendment to section 16 is meant to address an existing uncertainty regarding MOI amendments, it seems that even more questions may arise pursuant to the amendment.

SECTION 33 – THE ANNUAL RETURN

Every company must file an annual return, in Form CoR 30.1, with CIPC after the end of each anniversary of its date of incorporation. Form CoR 30.1 requires details of a company’s registered office, location of its records, directors, company secretary, auditors, financial year-end, its public interest score, principal place of business, holding company (if any) and whether it is required to be audited, among other things. All pretty innocuous. The new Act has, however, introduced a further controversial requirement, namely that, similar to section 26, a company is also obliged to file a copy of its financial statements if it was required to have them audited. Again, the controversial nature of this additional requirement is obvious, namely that this effectively renders a company’s AFS open for scrutiny by third parties. S33 also prescribes that the filing of the AFS with an annual return only applies to private or non-profit companies whose PIS “exceed the limits set out in s30(2) or the regulations contemplated in s30 (7) “. There are no such limits set out in Section 30(2) or Section 30(7). They deal with the requirement for a company’s AFS to be audited if its PIS exceeds a certain figure. I therefore interpret the amendment to means that a company need only file its AFS with its annual return if the AFS are required to be audited.

SECTION 38A – INVALID CREATION OR ISSUE OF SHARES

This is a new and welcome provision. It effectively provides that where a company purports to create, allot or issue shares by virtue of any provisions of the Act, its MOI or other lawful means but such creation, allotment or issue is, in fact, invalid or the terms of such creation, allotment or issue are inconsistent or not authorised by that provision, a court may, on application by the company or any person who holds an interest in the company and if it is

satisfied that it is just and equitable to do so, make an order validating the creation, allotment or issue of those shares or confirming the terms thereof, subject to such conditions as it may impose.

For example, if a company issued shares of a certain class in the *bona fide* belief that its MOI created such class of shares but this turned out to be incorrect, a court is now empowered to rectify the illegality on application by the company if it is satisfied that it is just and equitable to do so.

This is an example of easing the burden of doing business since the company would otherwise have to call a shareholders' meetings and propose new resolutions to its shareholders, among other things, to remedy the unlawful creation, allotment or issue of shares. It is to be welcomed in cases where innocent or tardy compliance with the formalities and/or record keeping requirements of law result in the irregular creation, allotment or issue of shares, especially where all shareholders are in favour thereof. In short, it seeks to give a court the power to remedy such a situation where there has been an "honest mistake".

It must be remembered that the current Section 38(2) provides that if a company issues shares that have not been authorised or in excess of the number of its authorised shares, such issue may be retrospectively authorised by way of a special resolution without the necessity to apply to court.

SECTION 118 – APPLICATION OF THE TAKEOVER PROVISIONS TO PRIVATE COMPANIES

This is the only amendment to the so-called Takeover provisions and Takeover Regulations, which are set out in section 117 to 127 of the Act and Regulations 81 to 122, the main purpose of which is to protect the general public and the minority shareholders of what is termed a "regulated company" where a regulated company is a party to, or is the subject of, a proposed fundamental transaction, such as a scheme of arrangement, or another transaction which, if implemented will result in a significant change in the holders of the voting securities of that regulated company. These are called "affected transactions".

The takeover provisions apply only to "regulated companies", namely public companies, state owned companies and private companies which satisfy the test set out in sections 118(1)(c) and (2). Before their amendment, these sections provided, among other things, that the takeover provisions apply to an affected transaction involving a private company or it's

securities if the percentage of the issued securities of that private company that had being transferred within the 24 months immediately before the date of the particular affected transaction exceeded 10%. The rationale seemed to be that, where a private company's securities were dealt in frequently or in significant blocks, the general public and it's minority shareholders require the protections that the takeover provisions offer.

This logic seems odd, to say the least. Why, for example, should the onerous and complex provisions of the takeover regime apply to a private company of whatever size just because, say, 30% of its shares changed hands over a 24 month period?

Thankfully, this test has now been abolished. In its place, we had a more practical and logical test in the new section 118(1)(c)(i), namely that a private company will be a "regulated company" if:

1. it has 10 or more direct or indirect shareholders; and

2. the private company meets or exceeds the financial threshold of annual turnover or asset value determined by the Minister in consultation with the Takeover Regulation Panel in general or in relation to specific industries.

These thresholds have not yet been published but we can expect them to be significant. They should limit the scope of application of the Takeover regime to private companies considerably.

The word "indirect" broadens the scope of this amendment and will thus result in more private companies being caught in the Takeover regime net.

The TRP is given the power to exempt any particular transaction involving such a private company.

SECTION 45 – FINANCIAL ASSISTANCE

Most companies were surprised (to say the least) when section 45 was enacted because of the exceptionally broad scope of its application and its practical effect. Its equivalent in the 1973 Act, section 226(1), applied only to directors, and in particular placed no restrictions on inter-group loans. Quite the reverse in fact. Section 37 expressly permitted a company to make a loan to a holding company, a subsidiary or a fellow-subsidiary.

Section 45 prohibits the granting of any form of financial assistance by a company unless the particular provision of financial assistance:

1. is pursuant to a special resolution of shareholders which approved its grant and was adopted within the previous two years;

2. satisfied the solvency and liquidity test immediately after providing the assistance;

3. the terms under which the assistance was proposed to be given were fair and reasonable; and

4. any conditions or restrictions respecting the granting of the assistance in the MOI were satisfied.

The problem with section 45 is the scope of its application. It applies to the provisions of "direct or indirect" financial assistance to:

1. a director or prescribed officer;

2. a director or prescribed officer of a company that is related or inter-related to the company;

3. a company that is related or inter-related to the company; and

4. a person who or which is related to the company or to any of the above persons.

Furthermore, the purpose of the assistance is irrelevant; the mere provision of financial assistance to, say, a holding company or a shareholder triggers section 45.

R. Jooste in the book "Contemporary Company Law", describes S45(2) as follows:

"The new provisions cast their tentacles far wider, drawing in a far more extensive range of transactions, as well as parties to such transactions, to which the provisions apply. The extent of this range is such that a vigilant, law-abiding company will be faced with an onerous task in assuring itself that it has complied with the law. It is submitted that the net has been cast too

wide, capturing situations that are no threat to the company in question, situations that do not involve any potential abuse of the powerful position of directors."

As a consequence of Section 45, it has now become common practise for most large companies, both public and private, forming part of a group of companies to table a special resolution at every AGM to approve loans to other companies forming part of the same group. The amendment to section 45 brings a measure of relief to this rather draconian and, given its scope, nonsensical provision by providing that section 45 does not apply to the giving by a company of financial assistance to or for the benefit of a subsidiary (as defined in the Act).

While this exemption is indeed welcomed, in my opinion it does not go nearly far enough. Why are fellow-subsidiaries also not exempted? Why are loans to holding companies not exempted? Why are foreign incorporated subsidiaries not exempted? In fact, it should exempt financial assistance to any group companies.

So, do not be fooled by the exemption. The spectre of section 45 still looms large as far as groups of companies are concerned, though it has been ameliorated to some degree.

SECTION 48 – SHARE BUY-BACKS

The Act provides for two forms of share buy-backs, namely the acquisition by:

1. a company of its own shares; and

2. a subsidiary of shares in its holding company.

If a company buys back its own shares, these shares must be cancelled because a company cannot own its own shares, whereas a subsidiary can hold shares in its holding company. Share buy-backs by a company of its own shares thus weakens the company because its share capital is reduced and, where shares are bought back for a material purchase price, it denudes itself of cash. In this sense, such a buy-back is tantamount to declaring a special dividend.

Share-buy backs place the directors of a company in an inherent conflict of interests position, especially if they all hold shares themselves. For instance, this inherent conflict affects the price at which the shares are repurchased or may even have an effect on control of the company.

It is for this reason that the JSE insists that any form of share buy-back be approved by the shareholders of the company by special resolution. It therefore came as a great surprise to most corporate lawyers that, when section 48 was first enacted, it did not contain the requirement for approval by way of a special or even an ordinary resolution of shareholders, even though certain exceptions and restrictions were introduced. These include the following:

1. a subsidiary cannot acquire more than 10% in aggregate of the number of shares of any class of its holding company and no voting rights attached to such shares may be exercised while held by a subsidiary;

2. the solvency and liquidity test in section 46 must be satisfied in all instances;

3. in order to protect minority shareholders, a special resolution is required if any shares are to be acquired by the company from a director or prescribed officer, or a person related to either of them;

4. If the buy back involves the acquisition by the company of more than 5% of the issued shares of any particular class, the requirements of sections 114 and 115 must be met. This means are that a share buy-back by the company of more than 5% of its issued shares is deemed to constitute a scheme of arrangement between the company and the holders of that class of shares and is thus subject to the onerous requirements of sections 114 and 115, including the sanction of independent shareholders by way of a special resolution. This requirement makes very little sense if the company is a small or medium sized company of if the company, no matter what its size, has only a few shareholders.

Thankfully, the Amendment Act has deleted the aforesaid 5% requirement. In its place, it has introduced a new requirement, namely that a special resolution of shareholders for the acquisition by a company of <u>any</u> of its shares is mandatory with two exceptions, namely:

1. where shares are acquired as a result of a pro-rate offer made by the company to <u>all</u> shareholders of a particular class, notwithstanding that the offer may include shareholders who are directors or prescribed officers; or

2. where it entails the acquisition of shares in the company as a result of transactions effected on a recognised stock exchange on which the company's shares are traded.

Note that the introduction of the special resolution requirement does not apply to the buy-back of shares by a subsidiary. This can this still be done without shareholder approval.

This is a positive change because it remove the burden of having to comply with section 114 and 115 and gives greater protection to shareholders in that the buy-back of even one share by a company now requires the sanction of a special resolution. It also simplifies the legislation.

SECTION 135 – LANDLORD'S RIGHTS WHERE THE TENANT IS IN BUSINESS RESCUE

Landlords and even tenants should welcome a long-awaited amendment to the business rescue regime. New section 135A is the only amendment to the provisions of the Act governing business rescue, which is surprising because there are numerous other provisions of Chapter 6 which requires amendment and/or expansion. Section 135A provides that all amounts for public utility services such as the company's share of rates and taxes, electricity, water, sanitation and sewerage charges which have been paid by the landlord to third parties during business rescue proceedings and which are due to a landlord under a contract (usually a lease) but which are not paid to the landlord are deemed to be post-commencement financing. These claims will be payable ahead of secured and unsecured claims against the company except for the practitioner's remuneration and employees' PCF claims and should therefore encourage landlords to not cancel leases, leaving the company with a better chance of survival.

SECTION 90 – AUDITORS

Every public company or state-owned company must have its AFS audited. In addition, a company whose PIS in a financial year is 350 or more, or whose PIS is at least 100 and it's AFS are internally compiled must have its AFS audited. Obviously, each such company must appoint an auditor. The auditor must, of course, be "independent" and must be appointed at a shareholders' meeting at which this requirement first applies to the company and thereafter annually at the shareholders' meeting. Companies which have an AGM will usually do so at the AGM.

Until now, a person could not be appointed as the auditor of a company if, during the 5 financial years immediately preceding the date of appointment, such person was a director or prescribed officer of the company or a person who, alone or with a partner or employees,

habitually or regularly performed the duty of accountant or bookkeeper or was an employee or consultant of the company who was engaged for more than one year in the preparation of any of its financial statements. The Amendment Act has reduced this 5 year period to 2 financial years. This change will therefore reduce the disqualification or “cooling off” period for a person to serve as a company's auditor, which is a welcome change.

SECTIONS 30 A AND 30 B – THE REMUNERATION POLICY AND REMUNERATION REPORT

This piece of new legislation has been by far the most controversial, highly debated provision of the amendments to the Act. The main reason for this is that the stances of business and labour on the topic were dramatically opposed. I will first take you through the legislation and then deal with these opposing views.

The first point to note is that sections 30A and 30B only apply to public companies and state-owned companies. It seems rather surprising that private companies who have large numbers of employees, of which there are numerous, are excluded. No doubt these companies will breathe a sigh of relief.

Section 30(4) of the Act requires that each company that is required by the Act to have it's AFS audited must include particulars showing the “remuneration” (as defined) and benefits received by each director or prescribed officer, as well as pensions paid by the company to current or past directors or prescribed officers, the amount paid or payable by the company to a pension scheme with respect to directors or prescribed officers, the amount of compensation paid to current or past directors or prescribed officers in respect of loss of office, the number and class of securities issued to a director or prescribed officer or any person related to them and the consideration received by the company for them, and details of service contracts of current directors and prescribed officers.

“Remuneration” is defined in section 30(6) as including directors fees, salaries, bonuses and performance related payments, expense allowances, contributions paid under any pension scheme not disclosed as set out above, the value of any option given directly or indirectly to a director, past director or person related to them, financial assistance to a director, past director or person related to them for the subscription of securities under section 44 and details of any loan or financial assistance by to a director or past director or future director if the company is a grantor of that loan.

These comprehensive AFS disclosure requirements have been in place since the Act first become law in 2011. However, while the word "remuneration" is extensively defined for purposes of compiling a company's AFS, it is not defined in Section 30A or 30B, but one would expect that companies will be required to give these or similar details when calculating a directors remuneration for purposes of section 30B. But it does beg many questions such as whether to include only South African employees, whether to include temporary employees, whether to include employees who have been outsourced to labour brokers, whether to report a group of companies as a whole or only as employees of subsidiaries or joint ventures, to name but some of them.

There is a new definition of "total remuneration" in section 30B, namely "all salary and benefits received including any employer contributions to benefit funds and any short-term or long-term incentives including share options and incentive awards."

King 4 recommends that the remuneration policy of a company be submitted to shareholders for consideration and for an advisory, non-binding vote to provide shareholders with an opportunity to indicate whether or not they support the material provisions of the remuneration policy of the company. The Act gives no definition of "remuneration policy", which is a pity. King 4 has a section dealing with remuneration policy which should prove to be a useful guide as to what the remuneration policy should deal with. "Policy" may be defined as a principle of behaviour or conduct thought to be necessary or desirable. For example, the process by which the board manages the determination of the remuneration of the directors.

As you know, most public companies and large private companies already have dedicated remuneration committees, again as recommended by King, which have the duty to oversee all aspects of remuneration of the company's directors and employees, and recommends that all members of it be non-executive directors with the majority being independent non-executive directors.

Section 30A deals with a company's remuneration policy. It provides that all companies must prepare a remuneration policy and present it to shareholders for approval by an ordinary resolution at the AGM. If it is not approved, it must be presented at the next AGM or at a shareholders meeting called for such purpose. The remuneration policy, when approved, will remain in force for 3 years from approval and must be again approved every 3 years thereafter. It may be amended prior to the end of the 3 year period but any material amendment can only be implemented after it is approved by shareholders by an ordinary resolution at an AGM or at a shareholders' meeting called for this purpose.

Since the remuneration policy need only be approved every three years, it will have to be a document which sets out the fundamental principles and philosophy applied by the company to remuneration, rather than dealing with matters such as performance targets for long and short term incentives, annual salary increases or the remuneration of non-executive directors and others.

The Amendment Act then goes on, in section 30B, to legislate for the preparation and presentation of a company's remuneration report. Section 30B(2), the operative section, provides that all companies must prepare a remuneration report each year in respect of the previous financial year for presentation and approval at the AGM. The report must comprise of a background statement, a copy of the remuneration policy and an implementation report containing details of:

1. the total remuneration received by each director and prescribed officer;

2. the total remuneration in respect of the employee with the highest total remuneration (usually the CEO);

3. the total remuneration in respect of the employee with the lowest total remuneration; and

4. the average total remuneration of all employees, median remuneration of all employees and the remuneration gap reflecting the ratio between the total remuneration of the top 5% highest paid employees and the total remuneration of the bottom 5% lowest paid employees.

It is the disclosure of the so-called “wage gap” which has proved to be the most controversial aspect of this legislation. More about that anon.

Sections 30B(4) and (5) then go on to provide for a so-called “2 strike” procedure. If the remuneration report is not approved by an ordinary resolution of shareholders, the remuneration committee must, at the next AGM, present an explanation in which the concerns of shareholders have been taken into account and those non-executive directors who serve on the remuneration committee must stand for re-election as members of the remuneration committee at that AGM. However, if at this second AGM, the remuneration report in respect of the previous financial year, is also not approved by shareholders, then the non-executive

directors who served on the remuneration committee may continue to serve as directors (if they are re-elected) but will not be eligible to serve on the remuneration committee for two years thereafter.

It is clear that the "two strike" system applicable to non-executive directors who sit on the remuneration committee will discourage failure to obtain shareholder approval, given the consequences thereof for such non-executive directors.

Sections 30A and B are good illustrations of two of government's goals, namely:

1. greater transparency of a company's activities; and

2. greater power for minority shareholders through the requirements for shareholder approval of the remuneration policy and the recommendation report, as well as the new pay gap reporting requirements.

Sections 30 A and B are not unique to South Africa. Similar legislation exists in other countries. There has for a number of years now been universal demands by the public, institutions and labour for greater transparency on executive remuneration, given the relatively enormous salaries and benefits which are frequently paid to senior executives. This is in stark contrast to the salaries paid to lower ranking employees and even to professionals such as doctors and engineers. There have thus been demands to narrow the pay gap between the highest and lowest paid employees, as recommended by the Zondo Commission.

From a corporate governance perspective, a lot of work will have to be done in amending governance documents and procedures. Matters such as delegation of authority, board charters and the terms of reference of board committees will have to be revisited. Of course, the resolutions proposed at the AGM will have to be changed to cater for shareholder approval of the remuneration policy and report. Also, the implementation report, which will form part of the remuneration report, will be a critical document because it must set out the "nitty gritty" critical disclosures which shareholders will undoubtedly pay close attention to.

In addition, and most importantly, the new requirements almost force a company's management to actively engage with stakeholders in order to attempt to get the consent of stakeholders to the policy and report prior to them being tabled at the next AGM. This is a good thing. For too long now, management has in many cases ignored the concerns of shareholders around excessive remuneration. The role to be played by institutions in this

regard is vital, given that they are invariably the largest minority shareholders in listed companies.

Apart from increased transparency and accountability, the objective of the new legislation is undoubtedly to aim to narrow the gap between the highest and lowest paid employees, particularly that of listed companies. Minister Patel has stated that the Act will help address SA's inequality issues. According to certain commentators, SA has the biggest income inequality in the world. In April 2023, the average nominal take-home pay was about R14,500. However, executives at certain of SA's major mining and banking companies, who I will not name, earned an average salary of R132 million per annum or about R11 million per month.

Minister Patel, in his commentary on the 2021 Bill, had this to say:

> "*The Bill attempts to strengthen the remuneration report provisions to provide more information to shareholders and stakeholders on the motivation for the remuneration of directors and prescribed officers, for transparency, accountability and good governance purposes.*
>
> *The amendments proposed in the Bill are also required to tackle the injustice of excessive pay. The pay gap has been a historical challenge in South Africa and a contributor to the country's inequality. Following this amendment, the Act will allow for stronger shareholder governance on excessive director pay and for companies, shareholders and stakeholders to be aware of and, if necessary, address unsustainable pay discrepancies.*
>
> *This kind of inequality underpins much of the well-known workplace conflict in South Africa. The proposed publication of indicators of pay differentials will empower shareholders and other stakeholders to see trends and, where warranted, propose changes. There are complex considerations of the appropriate pay-regime that should apply in a particular company; and due note should be taken of the need to attract and retain the best skills for domestic firms. The Bill does not seek to propose what the ratios between executive and worker pay should be; instead it proposes transparency and empowers shareholder voting to be more effective than is currently the case."*

From a "political" standpoint, the views on this new legislation have been varied. The NUM welcomes the legislation and commends government for making strides to ensure that companies recognise stakeholders participation. Afriforum, on the other hand, opines that the

amendments exacerbate the growing unease of directors and managers that are keeping the economy afloat and that they embarrass functional and practical business models. This, it says, will only serve to compel investors to reconsider the viability and sustainability of their financial position in SA and high-skilled workers to reconsider their future employment prospects in SA compared to other countries. Piet Mouton, the CEO of PSG, says the legislation will disadvantage listed companies because it does not apply to private companies; it creates an unlevel playing field. One portfolio manager blatantly said that the wage gap is irrelevant - "we already know that it is going to be atrocious, so I don't know what publishing it is going to achieve," he said. Other critics says that the amendments foist significant administrative burdens on public companies while diminishing SA's attractiveness as a place to do business. They argue that the new disclosure requirements may dissuade foreign companies from investing or remaining in SA. They say that we need to rather focus on improved education and job creation instead of witch-hunting which will ultimately harm the economy.

South Africa is a victim of the so-called "brain drain" that sees numerous skilled people leaving the country in pursuit of perceived better opportunities in foreign jurisdictions. If well qualified and experienced executives are unable to derive appropriate value for their services in South Africa because of the pressure brought to bear by section 30B, they may be incentived to consider off-shore opportunities.

The relative complexity applicable to the calculation of executive remuneration as compared to entry level employees may make reporting on the wage gap difficult, especially when considering that the executive incentives are often risk-based and dependent on a company achieving strategic goals or financial milestones over a period which may exceed a year. It is also unclear if the wage gap will be stated on a pre- or post-tax basis, which will impact the value of the remuneration ratio.

The practical consequences of a large wage gap, especially if this is coupled with an unapproved implementation, may "embarrass" a company, regardless of the nuances at play and the requirements and responsibilities of the particular roles that form part of the wage gap calculation.

Furthermore, reporting on the wage gap may incentivise companies to opt to outsource their employees in an effort to improve their wage gap. The Act also fails to balance the complexities of paying fair, market related remuneration against the financial sustainability of a company. In a country that has one of the highest unemployment rates in the world, reporting

on the remuneration of the highest paid employee against other metrics may be more appropriate, such as the total number of employees of the company, the total tax paid to SARS, the total remuneration paid to all employees of the company or some mechanism to take into account other contributions made by the company to the local or national economy in areas such as enterprise development or corporate social responsibility, or in the case of state-owned companies, success in providing improved services and infrastructure to the public at large.

On balance, the majority of sections 30A and B is a positive development for corporate governance that will align South African company law more closely with international best practise. This being said, and given the unique social economic position that South Africa is in, one wonders whether the unintended consequences of some of the requirements of section 30B are warranted, so as not to disincentivise suitably qualified people from serving as directors of public companies. This, in turn, may prejudice these companies and accordingly the shareholders, entry-level employees and prospective employees that section 30B seeks to protect.

The right balance between transparency and accountability needs to be met and the particular idiosyncrasies of the South African economy need to be taken into account. South African companies need the scope and autonomy to be able to incentivise executives - particularly given the overseas opportunities which are lucrative and attractive to local talent.

Ultimately, it is hoped that greater transparency will neither stifle companies' abilities to properly attract and retain people who are key to management and the strategy of the business, nor indirectly adversely affect employment at lower pay grade levels.

SECTION 72 – THE SOCIAL AND ETHICS COMMITTEE

Every listed public company, state-owned company and any other company that has, in any 2 of the previous 5 years, scored above 500 points of its PIS must appoint a social and ethics committee ("SEC") unless it is a subsidiary of another company that has a SEC or it has been exempted by the Companies Tribunal. An exemption is valid for 5 years.

The functions of the SEC are to "monitor the company's activities" with regard to matters relating to:

1. social and economic development, including the company's standing in terms of the goals and progress of, among other things, the Employment Equity Act and the BBBEE Act;

2. good corporate citizenship, including the company promoting equality, prevention of unfair discrimination and reduction of corruption and the company's contribution to development of the communities in which its activities are predominantly conducted or within which its products or services are predominantly marketed, as well as the company's record of sponsorship, donations and charitable giving;

3. the environment, health and public safety;

4. consumer relationships; and

5. labour and employment including the company's employment relationship and its contribution toward the educational development of its employees.

It must also draw matters within its mandate to the attention of the board when required and report, through one of its members, to the company's' shareholders at the company's AGM on the matters within its mandate.

The SEC must comprise of not less than 3 members, but:

1. in the case of a public company or SOC, the majority must be non-executive directors and must not have been involved in the day to day management of the company's business during the previous 3 financial years;

2. in the case of any other company, the members must consist of not less than 3 directors or prescribed officers, at least one of whom must be a non-executive director and must have not been involved in the day to day management of the company's business with the previous 3 financial years. This is the present position.

What is new is that the Act now requires that <u>a public company or SOC must elect a SEC at each AGM</u>. In the case of any other company required to have a SEC, the SEC must be appointed annually by its board of directors, which is the current position.

An additional new requirement is the obligation for a SEC to prepare a SEC report for shareholders detailing how it performed its functions in terms of the Act and the Regulations. This report must be presented:

1. in the case of a public company or SOC, at its next AGM;

2. in the case of any other company, annually at a shareholders meeting or with a Section 60(1) resolution (round robin resolution of shareholders).

Shareholders are not required to approve the SOC report.

SECTION 162 – DELINQUENT DIRECTORS

The Companies Second Amendment Act, which was published at the same time of publication of the Amendment Act, has its origin in the recommendations of the Zondo Commission of Enquiry into State Capture. It amends the Act by giving a court the power, on good cause shown, to extend the period during which proceedings may be commenced to recover any loss, damage or costs for which a person may be held liable in terms of section 77 for more than 3 years. Note that this power of extension is not limited to applications to declare a director delinquent; it applies to any civil claim under section 77, which is lengthy section governing the personal liability of directors for, among other things, breach of their fiduciary duties.

The new law also extends the time bar for declaring a director a delinquent director or under probation from 24 months to 60 months immediately preceding the application to court and even gives the court the power to extend the 60 month period on good cause shown.

This provision ensures that directors and prescribed officers can be held accountable for a significant longer period after they have committed unlawful acts.