

*A Sibanda*

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# The statutory remedy for unfair prejudice in South African company law

## Summary

The convergence of world economies as a result of globalisation calls for jurisprudential review relating to shareholder rights in various jurisdictions. Most countries, including South Africa, base the protection of minority shareholders on common law as well as “home-grown” legislation. Among its shareholder remedies, South African law provides the statutory remedy for unfair prejudice, also known as the “oppression remedy”. The remedy enables shareholders to seek judicial intervention when their corporate interests are jeopardized often by their majority counterparts. In the past, dissatisfied minority shareholders have utilised this remedy. This article considers whether the development of the remedy from its initial introduction in South African company law has been beneficial to shareholders. The author traces the history of the remedy to the *Companies Act* 46 of 1926 and its subsequent amendment in the *Companies Act* 61 of 1973 and *Companies Act* 71 of 2008, respectively. Recommendations on how the remedy can be further improved from its current form are also made.

## Die statutêre remedie teen onredelike benadeling in die Suid-Afrikaanse maatskappyereg

Die sameloop van die wêreld se ekonomieë as ‘n gevolg van globalisering het ‘n behoefte geskep vir ‘n juridiese hersiening van die regte van aandeelhouers in verskeie jurisdiksies. Die meeste lande, insluitend Suid-Afrika, baseer die beskerming van minderheidsaandeelhouers op die gemene reg, sowel as “tuisgemaakte” wetgewing. Die Suid-Afrikaanse reg maak, onder ander aandeelhouersremedies, voorsiening vir ‘n statutêre remedie teen onredelike benadeling, ook bekend as die “onderdrukkingsremedie”. Die remedie stel aandeelhouers in staat om geregtelike ingryping te bekom wanneer hul korporatiewe belange benadeel word deur gewoonlik meerderheidsaandeelhouers. In die verlede het minderheidsaandeelhouers hierdie remedie benut. Hierdie artikel ooweeg of die ontwikkeling van hierdie remedie vanaf die aanvanklike inkorporasie daarvan in die Suid-Afrikaanse maatskappyereg aandeelhouers enigszins bevoordeel. Die outeur ondersoek onderskeidelik die geskiedenis van die remedie in die *Maatskappywet* 46 van 1926 en die daaropvolgende wysiging daarvan in die *Maatskappywet* 61 van 1973 en die *Maatskappywet* 71 van 2008. Aanbevelings word ook gemaak oor hoe om die remedie verder te verbeter.

## 1. Introduction

Minority shareholder protection is a pertinent subject of company law.<sup>1</sup> Several countries continue to experience pressure to reform their corporate law remedies aimed at protecting the interests of minority shareholders. South Africa is among jurisdictions that base the rights of minority shareholders on common law and its domestic legislation. Being a part of the global economy, the country has responded to the plight of minority members by providing a statutory remedy which allows them to apply to court for relief if the affairs of the company, of which they are members, are being conducted, *inter alia*, in a manner that unfairly prejudices them. The remedy is a critical avenue whereby minority shareholders can protect their corporate interests. Judicial precedents reflect a steady balance between cases where the members have successfully applied for relief and instances where such applications have failed to survive the scrutiny of the court. Given this background, this article explores the question as to whether the progressive development of the remedy in South Africa is of significance to minority shareholders. The author discusses the remedy as it is presented in three separate Acts which form the foundation of contemporary South African company law, namely the *Companies Act* 46 of 1926, the *Companies Act* 61 of 1973 and the *Companies Act* 71 of 2008, respectively. The article also deliberates on how the remedy, particularly in the Act of 2008 can be made more protective to the interests of minority shareholders.

## 2. The remedy for unfair prejudice under the *Companies Act* 46 of 1926

The remedy for unfair prejudice was first introduced in South African company law with the adoption of section 111*bis*<sup>2</sup> in terms of an amendment to the *Companies Act* 46 of 1926 in 1952.<sup>3</sup> To obtain relief under the section, the applicant had to establish the following facts:

- that the affairs of the company were being conducted in a manner “oppressive to some part of the members”, including himself;

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1 LLB, LLM (UFH) PhD Candidate (Unisa). This article is inspired by the author’s LLM thesis completed in 2008 titled “A critical analysis of the remedy for unfair prejudice in terms of section 252 of the Companies Act 61 of 1973”. The author thanks all the anonymous reviewers for their valuable comments that assisted to improve the initial draft of the article.

2 Although section 111*bis* was primarily aimed at protecting the rights of minority shareholders, it was stated in *Benjamin v Elysium Investments (Pty) Ltd* 1960 (3) SA 467 (E) that an application under this section could also be brought by a member who shared voting control equally with another member. This view was confirmed in *Livanos v Swartzberg* 1962 (4) SA 395 (W).

3 See section 90 of the *Companies Amendment Act* 46 of 1926.

- that the facts would justify the making of a winding-up order on grounds that it was just and equitable to have the company wound up in terms of section 111(g) of the Act; but;
- that to wind up the company would unfairly prejudice the members being oppressed and;
- that the order the Court made could remedy the irregularity in such a manner that the company would continue to function properly and would in all probability not perish.<sup>4</sup>

Like section 210 of the English *Companies Act* of 1948, section 111*bis* was introduced as an alternative remedy to winding-up the company where a member(s) complained of oppression, a measure described in *Elder v Elder & Watson Ltd*<sup>5</sup> as “a cure that would be worse than the disease”. Prior to its introduction, the only available remedy for a disgruntled member was to apply for the winding-up of the company. However, an alternative remedy to winding-up could save minority members from other disadvantages associated with winding-up the company. For example, when the break-up value of the assets could be relatively small, this would result in the shareholders incurring a loss. Moreover, the only possible purchaser of the company’s assets available could be the very majority whose conduct had driven the minority to seek the redress of winding-up.

Whilst section 111*bis* was introduced to be utilised as an alternative to the harsh remedy of winding-up the company when a member contested some managerial issues, it was not aimed at eliminating the remedy of winding-up a company when peculiar circumstances could compel the court to do so.<sup>6</sup> There were cases where the company could be wound-up despite the existence of the lighter remedy provided in terms of section 111*bis*, for example, where the *substratum* of the company was gone.<sup>7</sup> This referred to a situation where the principal, main object or distinct purpose for which the company had been formed could no longer be pursued.<sup>8</sup>

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4 This requirement was not expressly stated in the Act. However, Reynolds J in *Irvin and Johnson Ltd v Oelofse Fisheries Ltd* 1954 (1) SA 241 (E) held that this was a factor which the petitioning member was also expected to prove.

5 [1952] SC 49.

6 On the other hand, it was held in *Scottish Cooperative Wholesale Society Limited v Meyer and Another* [1954] SC:381-393 that while the words of section 210 of the English *Companies Act* of 1948, which were similar to those of section 111*bis*, suggested that the legislature had in mind some remedy whereby the company, instead of being wound-up, would continue to operate, the object of the remedy was not to save the company from being liquidated, but to end the oppression of the petitioner by his counterparts.

7 *Taylor v Welkom Theatres (Pty) Ltd and Others* 1954 (3) SA 339 (O):350.

8 *Taylor v Welkom Theatres (Pty) Ltd and Others* 1954 (3) SA 339 (O):350. See also *Re Suburban Hotel Co* (1867) 2 Ch App 750 and *City Crushers Ltd v Central Crusher Supplies Ltd* 1933 TPD:111-116 where it was stated that the *substratum* of a company disappears when its object has become practically impossible to achieve and that, in justice to the members, it ought not to be allowed to continue to exist.

The *substratum* argument found considerable support, particularly in cases where the wrong pertained to the management of the affairs of the company.<sup>9</sup> Where a member applied for a winding-up order alleging lack of confidence in the conduct of the management of the company's affairs, his argument was supposed to relate solely to the conduct of the other members or directors in the scope of their duties and not in regard to their private lives or affairs.<sup>10</sup> Section 111*bis* did not also suspend any legitimate claims creditors could be having against the company.

## 2.1 The availability of the remedy to members of the company

The provisions of section 111*bis* could only be used by members of the company if they were jeopardized in their capacity as members.<sup>11</sup> Thus the member could not utilise the provisions of the section if he was affected, for example, in his capacity as a director, creditor or any other capacity.<sup>12</sup> Furthermore, only registered members, whose names had been entered into the members' register, had *locus standi* to apply for relief.<sup>13</sup> This excluded not only non-members, but also beneficial owners of shares who held their shares through nominees or trusts.<sup>14</sup> The nominee was the

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9 *Taylor v Welkom Theatres (Pty) and Others* 1954 (3) SA 339 (O):351; *Woomack v Commercial Vehicle Spares (Pvt) Ltd* 1968 (3) 422 (E).

10 See *Loch and Another v John Blackwood Limited* [1924] AC 788. There are, however, some other cases where the courts made a winding-up order, although the facts did not relate directly to the administration of a company's affairs. In *Lawrence v Lawrich Motors (Pty) Ltd* 1948 (2) SA 1029 (W), the court issued an order for the winding-up of a solvent company on the ground that the applicant's fellow director had committed adultery with the applicant's wife. In *In re Yenidje Tobacco Co Ltd* [1916] Ch 426, the court upheld an applicant's allegations of lack of confidence in a director arising from a "personal reason" and ordered that the company be liquidated.

11 Section 210 of the English *Companies Act* also provided for prejudicial conduct affecting members only in their capacity as members of the company.

12 See *Aspek Pipe Co Ltd & Another v Mauerberger & Ors* 1968 (1) SA 517 (C):525; Chadwick 1968:126. See also *Elder v Elder & Watson Limited*:49; Simmonds 1952-1964:1044; *Re a company (No 00709 of 1992)*; *O'Neill v Phillips* [1999] 2 All ER 961 973 (HL); *Re Lundie Brothers Ltd* [1965] 2 All ER 292; *Re Bellador Silk Ltd* [1965] 1 All ER 667; *Re a company (No 003843 of 1986)* [1987] BCLC:562-573; *Re Unisoft Group Ltd (No 3)* [1994] 1 BCLC 609-626; *Re JE Cade & Son Ltd* [1992] BCLC:213-229.

13 A person could become a member of a company in terms of the *Companies Act* 46 of 1926 by (a) subscribing to the memorandum of association; (b) having shares allotted to him; or (c) having shares transferred to him. Any person who subscribed to the memorandum of association or to whom shares had been allotted or transferred was supposed to be registered in the company's register of members to become a member of it. See section 27 of the *Act* of 1926.

14 The trustees or nominees of beneficial owners of shares were also required to have their names entered in the company's register of members to become members of the company. See section 27.

registered member who could apply for relief, but the person who was affected in the first instance was the beneficial owner.

## 2.2 The applicant was supposed to seek assistance in respect of oppressive conduct

Due to the difficulty in providing an exact definition of oppressive conduct, South African courts were guided by English case law adjudicated particularly under the then section 210 of the English *Companies Act* of 1948. Oppression pointed to a situation where the majority shareholders used their voting power unfairly in order to prejudice their minority counterparts or where they acted in a manner that made fair participation in the affairs of the company by minority members impossible.<sup>15</sup>

In the leading English case of *Elder v Elder & Watson Ltd*,<sup>16</sup> oppression was defined as conduct involving “a visible departure from the standards of fair dealing and a violation of the definitions of the conditions of fair play on which every shareholder who entrusts his money to a company is entitled to rely.” Likewise, in *Re Harmer Limited*,<sup>17</sup> oppression was described as “an unfair abuse of powers and impairment in the probity with which a company’s affairs are being conducted”. In *Scottish Cooperative Wholesale Society Limited v Meyer and Another*,<sup>18</sup> the court defined oppression to be “lack of probity and fair dealing in the affairs of the company to the prejudice of some portion of its members”.

A number of English law cases were instrumental in guiding South African courts to interpret the meaning of “oppression” in terms of section 111*bis* of the *Companies Act* 46 of 1926. In the case of *Aspek Pipe Co Ltd & Another v Mauerberger & Others*,<sup>19</sup> the court described “oppressive conduct” to be ranging from something “tyrannical”<sup>20</sup> to conduct contrary to conditions of fair play.<sup>21</sup> Likewise, in *Livanos v Swartzberg and Others*,<sup>22</sup> oppressive conduct was defined as any conduct that is “burdensome,

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15 The disputed conduct was supposed to involve an element of wrongfulness that prejudiced the minority.

16 *Elder v Elder & Watson Ltd* [1952] SC 49:55.

17 [1958] 3 All ER 669 (HL):689.

18 [1957] 3 All ER 66 (HL):86.

19 *Aspek Pipe Co Ltd & Another v Mauerberger & Others* 1968 (1) SA 517 (C):517. *Donaldson Investments (Pty) Ltd v Anglo-Transvaal Collieries Ltd and Others* 1979 (3) SA 713 (W):719.

20 See also *Marshall v Marshall (Pty) Ltd* 1954 (3) SA 571 (N) and *Porteus v Kelly* 1975 1 SA 219 (W).

21 See *Elder v Elder & Watson Ltd* [1952] SC 49:55.

22 1962 (4) SA 395 (W).

harsh and unfair” to the applicant,<sup>23</sup> a test applied in *Scottish Co-operative Wholesale Society Ltd v Meyer and Another*.<sup>24</sup>

The establishment of oppression in the context of section 111*bis* involved balancing the different rights and conflicting interests pertaining to majority and minority members, respectively, namely the exercise of majority voting power as opposed to the minority members’ right to fairly participate in the affairs of the company. To establish oppression in terms of section 111*bis*, it was not necessary that the majority had any expectation of pecuniary benefit when they implemented an oppressive resolution. Conduct could be oppressive, even though it was simply due to the controlling shareholder’s overwhelming desire for power and control.<sup>25</sup> Moreover, the underlying motive was not generally relevant to the enquiry.<sup>26</sup> To establish a case of oppression, the court considered the nature of the conduct in question and the effect which it had on other members of the company.<sup>27</sup>

### 2.3 The powers of the court under section 111*bis*

Section 111*bis* endowed the court with wide powers with regard to the remedies it could order to bring to an end the oppression complained of. The use of the words “such order it thinks fit” in the provision conferred a wide and unfettered discretion as to what order it could make, but subject to the overriding consideration that its order would aim to bring to an end the matters complained of.<sup>28</sup> Generally, in seeking to achieve this aim, the Court could make an order which could bear, either directly or indirectly, upon the author of the oppression.<sup>29</sup> He could be ordered to sell his shares to the oppressed, or to purchase their shares, or that the company’s memorandum of articles be altered so as to restrict his freedom of action within the company.<sup>30</sup>

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23 In deciding whether the respondent’s conduct was oppressive, the motive of the respondent was disregarded. The enquiry focused on the conduct itself and the effect it had on other members of the company.

24 *Elder v Elder & Watson Ltd* [1952] SC 49:71.

25 See *Re Harmer* [1958] 3 All ER 669 (HL):704.

26 *Aspek Pipe Co Ltd & Another v Mauerberger & Others* 1968 (1) SA 517 (C):529.

27 *Aspek Pipe Co Ltd & Another v Mauerberger & Others* 1968 (1) SA 517 (C):529.

28 Not “to bring to an end” to such an extent that the company cannot function. See *Irvin and Johnson Ltd v Oelofse Fisheries Ltd* 1954 (1) SA 241 (E):241. For criticism of this interpretation, see Oosthuizen 1981:223.

29 The section did not, however, grant the court the power to suspend the rights of the creditors of the company. See *Irvin and Johnson Ltd v Oelofse Fisheries Ltd* 1954 (1) SA 241 (E):243-244.

30 The provision by implication allowed the court to alter or add to the company’s memorandum and articles to remedy the complaint. Although this was not clearly stated in the provision, such an interpretation could be construed from sub-section (3) thereof.

### 3. The oppression remedy in terms of section 252 of the *Companies Act* 61 of 1973

The oppression remedy under the *Companies Act* 61 of 1973 was of major significance to minority shareholders. Following the review of South African company law by the Van Wyk de Vries Commission, which culminated in the promulgation of the *Act*, the remedy was expanded to give it a wider scope of application. Owing to its close relationship with the then antiquated section 111*bis* of the *Companies Act* of 1926, cases adjudicated under section 111*bis* remained relevant in interpreting the provisions of section 252. Similarly, English case law on the oppression remedy remained persuasive. Nevertheless, there were specific areas where the new provision differed with its predecessor.

The provision provided relief to members who proved that the affairs of the company were being conducted in a manner that was unfairly prejudicial, unjust or inequitable to them. Like its predecessor, section 252 was applicable to cases where the conduct in question constituted an exception to the rule outlined in *Foss v Harbottle*,<sup>31</sup> particularly the ability of the majority to bind the minority. Section 252 was used prominently in cases where majority shareholders abused their majority voting power to oppress minority shareholders.<sup>32</sup> However, the provision did not preclude an unfairly prejudiced member from applying for the winding-up of the company if it was just and equitable to wind it up in terms of section 344(h) of the *Act*.<sup>33</sup>

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31 Under this rule, the court is empowered to intervene in the management of a company in cases where majority shareholders sanction illegal transactions or actions, for example where a resolution that has to be endorsed by a special majority has, in fact, been endorsed by an ordinary majority, or if action is taken that is contrary to the memorandum or articles, or where the majority acts in a manner that constitutes “fraud on the minority” and where personal rights of members are prejudiced. See *Porteus v Kelly* 1975 (1) SA 219 (W):221C; *Taylor v Welkom Theatres (Pty) Ltd and Others* 1954 (3) SA 339 (O):351.

32 See *Garden Province Investment v Aleph (Pty) Ltd* 1979 (2) SA 525 (D):534; *Sammel and Others v President Brand Gold Mining Company Ltd* 1969 (3) SA 629 (A). Both cases, although adjudicated under different legislation, advocated for the definition of oppression within the context of instances where majority shareholders used their voting power to unfairly prejudice their minority counterparts.

33 For example, when there was a justifiable loss of confidence between members, see *Taylor v Welkom Theatres* 1954 (3) SA 339 (O); *Hart v Pinetown Drive-in Cinema Pty Ltd* 1972 (1) SA 464 (D):467; *Moosa v Mavjee Bhawan (Pty) Ltd* 1967 (3) SA 131 (T); *Loch v Blackwood Ltd* [1924] AC 783 (PC). Also when the *substratum* of the company had disappeared, see *Taylor v Welkom Theatres* 1954 (3) SA 339 (O):350; *Witwatersrand Deep Ltd v Union Mining and Finance and Investment Ltd* 1924 WLD 35:51-52.

An applicant in terms of section 252 was required to:

- establish that a specific act by the company or the majority members was “unfairly prejudicial, unjust or inequitable” to him as a member of the company; and
- establish that it was just and equitable that such an order be granted; and
- give an indication to the court of the type of order he preferred the court to make to end the oppression.

If the court was satisfied that the particular conduct<sup>34</sup> in question was in fact “unfairly prejudicial, unjust or inequitable”, as alleged by the complainant, or that the company’s affairs were being conducted in such a manner, the court could, if it considered it just and equitable, make such order as it thought fit to bring to an end the matters complained of.<sup>35</sup> Although the applicant could stipulate the kind of relief he preferred, this did not cripple the wide discretion conferred upon the court by section 252(3) in granting the relief it deemed fit to bring an end to the action complained of.<sup>36</sup>

### 3.1 Applicants in terms of section 252

The provisions of section 252 could only be utilised by a person who was prejudiced in his capacity as a member of the company.<sup>37</sup> A director, creditor or employee who was also a member of the company, could not institute action if he was affected in a capacity other than that of a member. The concept of membership under section 252 was interpreted in the light of the provisions of sections 103 and 104 of the *Companies Act* 61 of 1973. Section 103 listed persons considered to be members of a company upon entry of their names in the company’s register of members. The mere fact that someone owned shares in a company did not make him a member of the company. Similarly, a person who was the beneficial owner of shares that were registered in the name of another person in a representative capacity, for example, as trustee, curator or guardian, had no *locus standi* to apply for relief in terms of section 252.<sup>38</sup> The scope of the provision was subjected to criticism as being too restrictive and limited.<sup>39</sup>

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34 Which could be an act either of commission or omission by the company.

35 Section 252(3).

36 See *Breetveldt v Van Zyl* 1972 (1) SA 304 TPD:315; *Heckmair v Beton & Sandstein Industrieë (Pty) Ltd* (1) 1980 (1) SA 350 (SWA):353.

37 Like its predecessor, section 252 did not make provision for an action by directors, creditors or employees of the company who were not members of the company at the time of the application. See in *Ex parte Avondzon Trust (Edms) Bpk* 1968 (1) SA 340 (T):342 where the provisions of the old *Act* were dealt with.

38 See *Lourenco and Others v Ferela (Pty) Ltd and Others (No 1)* 1998 (3) SA 281 (T).

39 See *Oosthuizen* 1986:240. The author argued that a minority shareholder could be injured by his majority counterparts in a capacity other than that of a member, for example a person affiliated to the company as a director or a debenture-holder.



### 3.2 Unfairly prejudicial, unjust and inequitable conduct

A member could only complain of an act or omission on the part of the majority which was unfairly prejudicial, or unjust or inequitable to him as a member of the company. The use of the phrase “unfairly prejudicial, unjust or inequitable” conduct had the effect of giving section 252 a wider scope of application than its predecessor.<sup>40</sup> Section 111*bis* of the *Companies Act* 46 of 1926 allowed action only for conduct that was “oppressive”. Whilst the scope of section 252 was wider, the exact meaning of the words “unfairly prejudicial, unjust or inequitable” was somehow ambiguous.

In the leading case of *Donaldson Investments (Pty) Ltd v Anglo-Transvaal Collieries Co Ltd*,<sup>41</sup> the court highlighted that the use of the word “unfairly” in the provision was a qualification only of “prejudicial” and not also of “unjust or inequitable”, as it would be tautologous to speak of any act or omission as being unfairly unjust or unfairly inequitable.<sup>42</sup> It was also highlighted that the use of the word “and” in subsection 3 of the section made it necessary for an applicant to establish not only that a particular act or omission was unfairly prejudicial, unjust or inequitable, but also that it was just and equitable that the court makes an order in terms of subsection (3).<sup>43</sup>

In order to allow an application in terms of the provision, the court was supposed to be satisfied, objectively speaking, that the particular act was unfairly prejudicial, unjust or inequitable. Various tests previously used by the courts to determine whether a particular act was oppressive under section 111*bis*<sup>44</sup> were still applicable under the new provision. To determine whether conduct or a particular act is unfairly prejudicial, unjust or inequitable, the South African courts adopted a number of tests from English precedents.

First, the court would consider whether the conduct complained of involved “a visible departure from the standards of fair dealing and a violation of the conditions of fair play on which every shareholder who

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40 The onus of proof conferred on the applicant under this provision was also less onerous. See *Garden Province Investment v Aleph (Pty) Ltd* 1979 (2) SA 525 (D):531; *Donaldson Investments (Pty) Ltd v Anglo-Transvaal Collieries Ltd and Others* 1980 (4) SA 204 (T):209.

41 1979 (3) SA 713 (W):722.

42 1979 (3) SA 713 (W):722.

43 1979 (3) SA 713 (W):722.

44 The interpretation of the word “oppressive” under the old *Act* served as a point of departure in giving meaning to the phrase “unfairly prejudicial, unjust and inequitable” conduct under section 252. In *Garden Province Investment v Aleph (Pty) Ltd* 1979 (2) SA 525 (D):531, it was stated that cases decided under section 111*bis* as to the nature of the *onus* on the minority shareholder and as to what had to be proven by him before relief could be granted to him, applied *a fortiori* to the provisions of section 252.

entrusts his money to a company is entitled to rely”.<sup>45</sup> It was also considered whether the conduct revealed “a lack of probity and fair dealing”<sup>46</sup> or whether it could be described as “burdensome, harsh and wrongful”.<sup>47</sup> Another test was the one used in *Aspek Pipe Co (Pty) Ltd v Mauerberger*,<sup>48</sup> where it was stated that an applicant was to establish that “the majority shareholders are using their greater voting power unfairly in order to prejudice him, or are acting in a manner which does not enable him to enjoy a fair participation in the affairs of the company”. The test used in the *Aspek Pipe Ltd*<sup>49</sup> decision was easier to apply, considering that it focused mainly on an *abuse of voting power* by majority members that prejudiced their minority counterparts rather than directly attacking a particular act which could have been endorsed by majority shareholders.

The application of various tests of unfair prejudice after a particular decision had been approved by majority members was usually problematic, considering the entrenchment of majority rule as a fundamental principle of corporate democracy. This predicament was addressed in *Sammel v President Brand Gold Mining Co Ltd*<sup>50</sup> where it was stated that:

by becoming a shareholder in a company a person undertakes by his contract to be bound by the decisions of the prescribed majority of shareholders, if those decisions on the affairs of the company are arrived at in accordance with the law, even where they adversely affect his own rights as a shareholder.

The *dictum* recognized the rule of the majority and the protection of minority shareholders as separate concepts that run parallel to each other, subject to an underlying understanding that the majority could not use its voting power to abuse minority members. Moreover, whilst majority rule was a respected principle of corporate governance, minority shareholders could only be bound by the decisions of their majority counterparts if those decisions had been arrived at legally. The learned judge’s comment described unfairly prejudicial, unjust or inequitable conduct as any course of conduct that amounted to an abuse of majority rule and that was contrary to accepted standards of business ethics, and which was aimed at compelling their minority counterparts to conform to their questionable

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45 This test was first applied in *Elder v Elder and Watson Ltd* [1952] SC 49:55, 60. It was also reiterated in *Re Harmer Ltd* (1958) 3 All ER 701:702.

46 This test was construed from *Elder v Elder and Watson Ltd* [1952] SC 49:55, 60. It was later applied in various South African cases, for example *Aspek Pipe Co (Pty) Ltd v Mauerberger* 1968 (1) SA 527.

47 This test was originally applied in *Scottish Cooperative Wholesale Society Limited v Meyer and Another* [1957] 3 All ER 66 (HL).

48 1968 (1) SA 527.

49 1968 (1) SA 527.

50 *Sammel and Others v President Brand Gold Mining Company Ltd* 1969 (3) SA 629 (A):678.

wishes. This resembled the test for unfairly prejudicial conduct that was adopted in *Aspek Pipe Co (Pty) Ltd v Mauerberger*.<sup>51</sup>

Majority members are obliged to use their power *bona fide* for the benefit of the company as a whole.<sup>52</sup> Thus, lack of confidence in the manner in which the company was being run, resentment at being outvoted or mere disgruntlement in the way the affairs of the company were being conducted did not amount to unfair prejudice in the context of the section.<sup>53</sup> If no benefit to the company could be derived from a particular transaction that was favoured by the majority, it could, on the other hand, be evidence of oppression of minority members. While this test was useful, it was not unilaterally applied in investigating oppressive conduct. Other tests were jointly applied with it, particularly those adopted from *Scottish Cooperative Wholesale Society Limited v Meyer and Another*<sup>54</sup> and *Elder v Elder & Watson Ltd*,<sup>55</sup> which served as useful guides for the courts in interpreting the concept of unfair prejudice.

When determining whether a particular course of conduct was unfairly prejudicial, unjust or inequitable in terms of section 252, the underlying motive of the oppressors was relevant but only as an aid to the court to arrive at a conclusion.<sup>56</sup> It is also important to note that the court observed whether the conduct and its consequences were unfairly prejudicial, unjust or inequitable to the applicant.<sup>57</sup> This approach was also heavily criticised by legal scholars.<sup>58</sup> There was a need for the court to have the power to come to the assistance of a minority member where the majority's action was clearly unfairly prejudicial, unjust or inequitable without waiting for the effects. The wording of section 252 itself focused on the *act* or *omission*, or

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51 1968 (1) SA 527.

52 See *Gundelfinger v African Textile Manufacturers Ltd* 1939 AD 314:324-325; *Sammel v President Brand Gold Mining Co Ltd* 1969 (3) SA 629 (A); *Garden Province Investment v Aleph (Pty) Ltd* 1979 (2) SA 525 (D):531-532; *Donaldson Investments (Pty) Ltd* 1979 (3) SA 713 (W):723; *Allen v Gold Reefs of West Africa* [1900] 1 Ch 656. The test in *Sammel v President Brand Gold Mining Co Ltd* was criticised by some authors as an unsatisfactory way of proving oppression. Nevertheless, although the test was regarded as inadequate, its major advantage was that it put the conduct of majority members under the strict scrutiny of other members instead of being overshadowed by the mere fact that the will of the majority always prevailed.

53 See *Garden Province* 1979 (2) SA 525 (D):535.

54 [1957] 3 All ER 66 (HL).

55 [1952] SC 49.

56 See *Ben-Tovim v Ben-Tovim and Others* 2001 (3) SA 1074 (C):1091; *Aspek Pipe Co Ltd v Mauerberger* 1968 (1) SA 527:529; *Garden Province Investment v Aleph (Pty) Ltd* 1979 (2) SA 525 (D):531; *Donaldson Investments (Pty) Ltd v Anglo-Transvaal Collieries Ltd and Others* 1983 (3) SA 96 (A):111.

57 See *Garden Province Investment v Aleph Pty Ltd* 1979 (2) SA 525 (D):531; *Ben-Tovim v Ben-Tovim and Others* 2001 (3) SA 1074 (C):1091.

58 See Van Rooyen 1983:434-443; Oosthuizen 1981:230; Hurter 1997:208-209. According to the latter, the requirement for the applicant to prove that the alleged act and the consequences thereof were prejudicial brought an unnecessary burden of proof.

the *affairs of the company being conducted* in a *manner* that was unfairly prejudicial, unjust or inequitable. The provision did not cater for conduct that later turned out to have the effect of being unfairly prejudicial, unjust or inequitable.

Section 252 was not applicable to expected or threatening conduct. In *Porteus v Kelly*,<sup>59</sup> the court rejected an application by a shareholder under section 252 for an interdict against majority shareholders from passing a resolution which the applicant alleged to be potentially oppressive. The court submitted that section 252 did not empower it to prevent a resolution from being passed, but only to intervene in respect of conduct that had been fully performed.<sup>60</sup> Similarly, the applicant could not base his application on allegations that an investigation would possibly reveal that the affairs of the company were being conducted in a manner that was unfairly prejudicial, unjust or inequitable to him.<sup>61</sup> A member applying for relief in terms of section 252 had the burden of proving, on a balance of probabilities, *conduct on the part of the majority* that was unfairly prejudicial, unjust or unfair to him.

### 3.3 Remedies available to members under section 252

The court could make any order it deemed fit under section 252 with the view to bringing an end to the matters complained of. The order made was supposed to have the effect of ending the oppression of the applicant. In most cases, the courts ordered other members to buy the shares of the complainant.<sup>62</sup> Usually the majority were ordered to buy out the minority, although the reverse could also be ordered. Where such an order was granted, the court had an unfettered discretion as to the method of fixing the price of the shares.<sup>63</sup> There was no rule of universal application for valuing of shares and the *Act* contained no express guidelines which the court could apply. This was so because different valuation methods were applied depending on the circumstances and merits of each case. Most of the valuation methods were developed under English law and remained influential in this regard. The few reported South African cases, in which the courts ordered an applicant to be bought out by the other shareholders, did not reflect the exact methods used by the court to arrive at a fair value of the shares.

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59 1975 1 SA 219 (W).

60 The prejudicial act was supposed to have been carried out by a resolution being passed by the required majority.

61 See *Investors Mutual Funds Ltd v Empisal (South Africa) Ltd* 1979 (3) SA 170 (W):176.

62 The court could also order that a beneficial owner buy the shares of the complainant. See *Re a company* [1986] 2 All ER 253.

63 The process of valuing shares usually involved the expertise of an independent auditor.

The court could also order the sale of the company's assets in order to enable a member who was being prejudiced as contemplated by section 252 to be paid the consideration for his interest and termination of his membership. In a related case of *Gatenby v Gatenby and Others*,<sup>64</sup> the court ordered that a hotel run by a close corporation be sold to pay out to a member, his interest and consequently to bring about termination of his membership in the corporation. The application was lodged in terms of section 49 of the *Close Corporations Act* 69 of 1984, which was much similar to section 252 of the *Companies Act* 61 of 1973 and also conferred a wide discretion upon the court to grant an order it deemed fit to end the oppression of the applicant.

Other orders the court could issue and that affected the future operation of a company included an order that the company's capital be reduced or that its articles be altered. It, however, remained unclear whether South African company law allowed the court to grant an interdict in favour of the applicant under section 252.<sup>65</sup> Moreover, the provision did not stipulate whether the nature of relief offered to the applicant under it was required not to have a crippling effect on the future operation of the company.

#### 4. The remedy for unfair prejudice in terms of the *Companies Act* 71 of 2008

The remedy for unfair prejudice is provided in terms of section 163 of the recently introduced *Companies Act* 71 of 2008. In terms of the provision, a shareholder or a director of a company may apply to a court for relief if:

- any act or omission of the company, or a related person, has had a result that is oppressive or unfairly prejudicial to, or that unfairly disregards his or her interests;
- the business<sup>66</sup> of the company, or a related person, is being or has been carried on or conducted in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards his or her interests; or
- the powers of a director or prescribed officer of the company, or a person related to the company, are being or have been exercised in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards his or her interests.

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64 1996 (3) SA 118 (E).

65 The wording of the section, however, implied that the remedies the court could grant in terms of it did not constitute a comprehensive list.

66 See Cassim *et al.* 2012:765-766 for a discussion on the difference between the "business" and "affairs" of the company. The author argues that the "business" of a company is a much narrower concept than its "affairs".

## 4.1 Applicants under section 163

Section 163 of the *Companies Act 71 of 2008* extends the *locus standi* of applicants not only to shareholders, but also to directors of the company. In terms of the previous *Act*, only members or shareholders of the company could apply for relief from oppressive or unfairly prejudicial conduct. In terms of the preceding provision, an applicant had to prove that he has been injured in his capacity as a member of the company and not, for instance, as a director or in some other outside capacity. The provision also denied relief to persons who held shares in the company, but who were not yet registered as its members or shareholders. Similarly, section 163 requires that a party who brings an action in the capacity of a shareholder should be registered as such. In terms of the *Act*, a shareholder is defined as “the holder of a share issued by a company and who is entered as such in the certified and uncertified securities register, as the case may be”.<sup>67</sup> In *Lourenco v Ferela*,<sup>68</sup> a case decided under the old *Act*, the applicants were regarded to be lacking legal standing, although they had inherited shares but were not yet registered as shareholders of the company.

Section 163 also entitles directors to seek relief from “oppressive or prejudicial conduct” under its provisions. The definition of a “director” in the *Act* encompasses an alternative director or any person occupying the position of a director or alternative director, by whatever name that the person may be designated.<sup>69</sup> A *de facto* director would consequently also appear to qualify for relief under the section.<sup>70</sup> The accommodation of directors in the scope of section 163 caters for quasi-partnerships where members occupy management positions and receive their investment returns in the company through remuneration. Where the applicant is a director, the conduct in question should have affected him in such capacity and not, for instance, as a creditor.<sup>71</sup> The provision does not only cater for a breach of the rights of the applicants, but also their interests which is a wider concept. The quasi-partnership type of case serves as a useful illustration of the distinction between “rights” and “interests”.<sup>72</sup> A quasi-partnership is established with an underlying arrangement that members will participate in the management of the company. It follows that where a shareholder or quasi-partner is forced out of his office by the exercise of majority voting power by his counterparts, this will affect not only his rights but also his interests as a shareholder.<sup>73</sup> Section 163

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67 Section 1 of the *Companies Act 71 of 2008*.

68 1998 (3) SA 281 (T).

69 Section 1 of the *Companies Act 71 of 2008*.

70 Cassim *et al.* 2012:760.

71 Cassim *et al.* 2012:760; Delpont *et al.* 2011:567.

72 Cassim *et al.* 2012:762.

73 Interestingly, the interpretation of the “interests of members” under the oppression remedy in terms of the English *Companies Act* of 2006 encompasses not only interests derived from membership, although they must be reasonably connected to such. See *Gamlestaden Fastigheter AB v Baltic Partnership Ltd v Baltic Partners Ltd* [2007] UKPC 26, [2007] Bus LR 1521.

appears to be affording a disgruntled quasi-partner the choice to lodge a complaint as shareholder or director of the company.

## 4.2 Objectionable conduct under section 163

An applicant under section 163 should first prove “a conduct”, which can be:

- a commission or omission by the company or another entity related to it,<sup>74</sup> or
- the conduct or carrying on of the business of the company or a related person, or
- the exercise of powers by a director or a prescribed officer of the company or related entity.

Section 163 eliminates the additional evidential requirement provided by its predecessor, namely that the applicant had to establish that it was “just and equitable” for the court to make an order under the oppression remedy.<sup>75</sup> In the context of the provision, what matters is the result of the act or omission, that is, whether it resulted in oppression or unfair prejudice or disregard of the interests of the applicant.<sup>76</sup> Similarly, section 252 of the repealed *Act* focused on the effect of the act rather than its underlying motive.<sup>77</sup> An act by an individual authorised by the board, for example a managing director, also falls within the ambit of this provision. Prescribed officers whose powers may form the subject of section 163 include persons who, despite not being directors of the company, enjoy some degree of executive authority.<sup>78</sup> A shareholder resolution in a general meeting fits in the definition of “acts of the company”. Section 163 covers isolated as well as continuing acts, but excludes threatened conduct. The conduct anticipated by the provision includes acts by the company or an entity related to it which captures a “holding-subsidiary” relationship

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74 A related person or entity, as defined in section 2 of the *Act*, includes a holding company and subsidiary relationship as well as the direct or indirect control of another company or its business by a third entity.

75 The requirement was unnecessary, as it brought an onerous burden of proof upon the applicant. Where a case of unfair prejudice is proven by the applicant, the court should be automatically compelled to render justice to the affected party by making a suitable order. Cassim *et al.* (2012:764) argue that, although the “just and equitable” requirement has been dispensed with in the new *Act*, it is likely to be considered by the courts in interpreting the provision, for example, where the conduct in question falls within the ambit of the *de minimis* principle.

76 A similar position prevails in other jurisdictions such as England, Australia and New Zealand.

77 *Ben-Tovim v Ben-Tovim and Others* 2001 (3) SA 1074 (C):1091; *Aspek Pipe Co Ltd v Mauerberger* 1968 (1) SA 527:529; *Garden Province Investment v Aleph (Pty) Ltd* 1979 (2) SA 525 (D):531; *Donaldson Investments (Pty) Ltd v Anglo-Transvaal Collieries Ltd and Others* 1983 (3) SA 96 (A):111.

78 Cassim *et al.* 2012:767.

between juristic persons. In the English decision of *Scottish Cooperative Wholesale Society Limited v Meyer and Another*,<sup>79</sup> it was emphasised that the relationship between related entities should be a fair one, particularly with the holding company dealing with its subsidiary in a just manner. A similar approach is adopted in interpreting the provisions of section 163.<sup>80</sup> Contrary to the new provision, section 252 of the *Act* of 1973 required the applicant to complain of conduct by the company in which he or she is a shareholder.

### 4.3 Oppressive, unfairly prejudicial or unfairly disregards the interests of the applicant

An applicant under section 163 has to prove that the conduct in question is “oppressive” or “unfairly prejudicial to the applicant” or “unfairly disregards the interests of the applicant”. This judicial construction gives the provision a wider scope of application, but its ambit remains undefined in the *Act*. Section 241 of the *Canada Business and Corporations Act*, which contains similar expressions, may have influenced the crafting of section 163 of the *Companies Act* of 2008. Canadian courts have treated the terms as symptomatic of solitary and broad standard of conduct which, if breached, instigates action for relief.<sup>81</sup> Considering that the terms “oppressive” and “unfairly prejudicial” have been used in previous South African legislation, namely the *Act* of 1926 and the *Act* of 1973, respectively, cases adjudicated under them provide an interpretive guide for the application of the provisions of section 163.

A key development brought by section 163 is its focus on conduct that “unfairly disregards the interests of members”. This wording expands the scope of impeachable corporate conduct, unlike the preceding provision that only focused on “unfairly prejudicial conduct”. Moreover, reference by the provision to conduct that “unfairly disregards the interests of members” captures “legitimate expectations” of members that may need to be protected in certain cases. “Legitimate expectations” were recognised in *Ebrahimi v Westbourne Galleries Ltd*<sup>82</sup> as a legally recognised class of shareholder rights. Such rights emanate from a mutual understanding or agreement which, although not necessarily incorporated in the articles of the company, form a basis on which the company’s affairs are conducted. This is common in privately owned companies.<sup>83</sup> Where a member alleges violation of his legitimate expectations, the court adopts an objective

79 [1957] 3 All ER 66 (HL).

80 In terms of section 76 of the *Companies Act* 71 of 2008, directors also have fiduciary duties to subsidiary companies of the holding company. See Havenga *et al.* 2012:132 for a discussion on the use of section 163 by directors or shareholders of subsidiary entities under the *Companies Act* of 2008.

81 See *Westfair Foods Limited v Watt* (1991) 79 DLR (4<sup>th</sup>) 48:52, *Ferguson v Imax Systems Corporation* (1983) 43 OR 128:137.

82 [1973] AC 360:378-379.

83 Also referred to as *quasi*-mutual partnerships.



approach, and examines the effect of the conduct on the member, as considered from the perspective of a reasonable bystander.<sup>84</sup> In publicly owned companies, there is usually no underlying personal relationship between members that determines how the affairs of the company will be conducted. It becomes difficult in such cases to apply the concept of legitimate expectations.<sup>85</sup>

#### 4.4 Court remedies under section 163

The court is provided with an unlimited discretion in terms of section 163(2) to make a suitable remedy to assist the complainant.<sup>86</sup> To encourage an open-ended approach, section 163(2) uses the word “including”, indicating that the court is not confined to the list of remedies given in the section. The range of orders that may be made by the court under section 163(2) are wide and some of them have far-reaching consequences, for example, an order for the amendment of a shareholder agreement as well as the setting aside of the agreements or transactions of the company with third parties. The *Act* was, however, careful to retain remedies that will encourage minimum judicial intervention in the management of the company, for example, any order for the aggrieved shareholder to be compensated by the company.<sup>87</sup> The provision also empowers the court to issue interim orders in some situations.<sup>88</sup> Interim orders by the court will prevent further prejudice of applicants’ interests pending the finalisation of an application for relief under the provision.

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84 That is, whether a reasonable bystander observing the consequences of the conduct of the controlling member(s) could regard it as having unfairly prejudiced the petitioner’s interests. A subjective element to the test was introduced in Australia which required the reasonable bystander to possess special skills or knowledge possessed by the oppressors. See *Wayde v New South Wales Rugby League Ltd* (1985) 10 ACLR 87 96:806-807.

85 See *Re Blue Arrow plc* [1987] BCLC 585. The applicant’s complaint was that she had been removed from her position as non-executive president of the company which was publicly-owned. She failed to establish any expectation that she would not be removed from office by alteration of the articles of the company. The court held that it was impossible in public companies to derive any legitimate expectation to remain president from arrangements outside those embodied in the constitution of the company, since outside investors were entitled to assume that the entire constitution was contained in the articles read in conjunction with legislation.

86 See section 163(2) for a list of orders the court can make.

87 *Cassim et al.* 2012:774.

88 See *Kudumane Investment Holding Ltd v Northern Cape Manganese Company (Pty) Ltd & 2 others* 2012 SA (GSJ); *Grancy Property Limited v Manala* (665/12) [2013] ZASCA 57.

## 5. Recommendations

The oppression remedy remains a crucial mechanism to safeguard the interests of shareholders. It is against this background that the amendment of the remedy in the recent reformation of South African company law is welcomed. An analysis of section 163, however, indicates that the remedy can be further improved if the following aspects are given due consideration.

### 5.1 The *locus standi* of unregistered securities holders

The *locus standi* of applicants under the provision should not only be limited to registered shareholders of the company. Holders of a beneficial interest in shares, although not formally yet registered with the company, should be considered under the provision, as they have legitimate corporate interests which can be harmed prior to them becoming registered members. Confirming this argument, Poon and Loh submit that modern stock markets are characterised by persons who purchase shares through stock exchanges and do not bother to register themselves because of the length of time involved.<sup>89</sup> Although the law provides for such beneficial owners to be registered or compel their nominees to lend their names to the proceedings, the process may be long so that, by the time it is done, the wrongful act complained of may have been completed or the protection afforded by the oppression remedy will have been lost.<sup>90</sup> In that respect, South Africa can consider the Canadian approach which extends the oppression remedy to beneficial owners of securities in a company or its affiliates.<sup>91</sup> Similarly, section 994 of the English *Companies Act* of 2006 provides for the use of the oppression remedy by “a person who is not a member of a company but to whom shares in the company have been transferred or transmitted by operation of law as they apply to a member of a company.” To qualify for relief under section 994, the applicant must show that he has agreed with the existing member for the transfer of shares to bind himself, and that a proper instrument of transfer in respect of those shares has been delivered to the transferee or the company.<sup>92</sup> Similarly, the *Companies Act* of 2008 makes provision for such an approach, as section 51(6) of the legislation provides for the recognition of transfer of certified securities upon the delivery of the share certificate to the company.

### 5.2 Anticipated oppression

Section 163 does not allow members to apply for relief in respect of proposed acts that may harm their interests. It follows that the court

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89 Poon & Loh 1980:296.

90 Poon & Loh 1980:297.

91 See section 238 of the Canada *Business Corporations Act*, R.S.C. 1985.

92 Joffe *et al.* 2011:240.

should have the power to come to the assistance of a minority member where proposed action by the majority or any other influential people in the company is clearly unfairly prejudicial, unjust or inequitable, without having to wait for its effects. The possibility of including anticipated oppressive acts within the scope of the oppression remedy in South Africa is supported by both academic arguments and other jurisdictions that serve as examples. Koehnen compellingly argues that a case of threatened oppression may actually be prejudicial to a member's existing interests.<sup>93</sup> Furthermore, the underlying purpose of the oppression remedy is viewed as being to "prevent misconduct as much as to redress it".<sup>94</sup> Regarding jurisdictional developments that support the prevention of potentially oppressive conduct, the oppression remedy in Australia and England provide emulatable examples. Sections 232 to 235 under Part 2F.1 of the *Corporations Act* of 2001 extends the applicability of the oppression remedy to an "act or omission, or a proposed act or omission, by or on behalf of the company".<sup>95</sup> Similarly, section 994(1)(b) of the English *Companies Act* of 2006 enables members to seek for relief when they anticipate any oppressive conduct.

## 6. Conclusion

The oppression remedy remains one of the powerful statutory inroads into the exercise of majority power by shareholders. Minority shareholders have been able to use the remedy effectively in jurisdictions where it is extensively developed to give courts the freedom to interpret it widely with the view of granting justice to affected shareholders. In Canada, the wide nature of the oppression remedy and its liberal interpretation by courts have given it the ability to be favoured by the bulk of disgruntled minority shareholders at the expense of alternative remedies such as derivative action or just and equitable liquidation.<sup>96</sup> Considering that majority rule is an axiomatic doctrine of company law, various jurisdictions have to consider how they can develop the oppression remedy as a means to prevent its arbitrary use. Against this background, the progressive reformation of the oppression remedy in South Africa, which culminated in its amendment in the *Companies Act* 71 of 2008, is welcomed as a necessary stride towards commendable minority shareholder protection. Nevertheless, there is room for section 163 to be further developed in light of the experiences of other jurisdictions explored in the article. Such reformation will allow courts to exercise judicial creativity as they grant justice to minority shareholders in the context of the complexities of modern companies. As a point of departure, the oppression remedy in South Africa should consider incorporating the interests of unregistered holders of securities and cases of anticipated oppression.

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93 Farley *et al.* 2007:291, citing Koehnen 2004:51.

94 Farley *et al.* 2007:291, citing Koehnen 2004:51.

95 See also section 181 of the *Companies Act*, A125, of Malaysia which provides for the use of the oppression remedy in respect of anticipated oppressive acts.

96 Farley *et al.* 2007:262.

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