Regulation of takeovers and mergers with an emphasis on the mandatory offer rule: a comparative and critical analysis of the law and the institutions that have been set up to enforce the law

by

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Declaration

By submitting this dissertation electronically, I declare that the entirety of the work contained therein is my own, original work, that I am the sole author thereof, that reproduction and publication thereof by the Stellenbosch University will not infringe any third party's rights and that I have not previously in its entirety or in part submitted it for obtaining any qualification.

Summary

This dissertation assesses the regulation of takeovers and mergers and the institutions created to enforce the law, from a comparative perspective. It uses South Africa as its point of departure and takes the laws of Delaware in the United States, the United Kingdom and Australia into account. The dissertation indicates that numerous takeover provisions in South Africa are poorly formulated, making them difficult to interpret and apply. Accordingly, the dissertation recommends amendment and improvement of certain Takeover Provisions.

Special emphasis is placed on the mandatory offer requirement. The dissertation critically and comparatively analyses this requirement and especially its impacts on the market for corporate control, efficient usage of capital, corporate governance and (in South Africa) Broad Based Black Economic Empowerment.

It appears from the literature explored that the mandatory offer requirement originated from the *Perlman* case in the United States as an expression of the equal opportunity rule. According to the equal opportunity rule, the controlling stake of a company is enriched with a premium of control, which must be shared with other shareholders when there is a change of the controlling shareholder. Shareholders must be given an equal opportunity to share in this control premium. Hence, a mandatory offer must be made to the remaining shareholders of the company by the new controlling shareholder at a price at which control was bought. *Perlman* case was decided in the United States of America during 1955.

It is contended in the dissertation, that the mandatory offer requirement in section 123 of the Companies Act 71 of 2008 (“the Act”), can ultimately be traced back to this case. Researchers have criticised the mandatory offer requirement in a number of respects. It has been pointed out that the rationale for the decision in the *Perlman* case was not clear and applied in limited circumstances. Other scholars point out that the case was

not a final decider on the sharing of the control premium due to later judicial pronouncements that differed with that case. Despite these commentaries, it appears that the case became a basis for imposing and enforcing this most debated rule in takeover and merger law.

The dissertation concludes that the sharing of a premium of control, as envisaged by the mandatory offer requirement, is not enforced in the state of Delaware. It further concludes that in the UK, the mandatory offer rule forms the cornerstone of enforcement of the equal opportunity rule, but that widely dispersed shareholding ameliorates it negative consequences in that jurisdiction. The dissertation favours the Australian approach. That jurisdiction does not require a mandatory offer similar to that in section 123 of the Act, but, Australian Takeover Provisions, unlike their South African equivalent, have been tailor-made for Australian market conditions. The dissertation accordingly concludes that the mandatory offer requirement in section 123 of the Act in its current form is not appropriate for South Africa.

Kakaretšo

Sengwalwa se sa nyakišišo se sekaseka melao le taolo ya gotšewa le gohlakantšhwa gadikhampani, gotee le metheo e hlomilwego gore melao e phethagatšwe, ka go bapetšwa. Sengwalwa nyakisišo se, se šomiša Afrika Borwa bjalo ka seikokotlelo sa sengwalo ebile se sekegela tsebe melao ya Mmušong waDelaware gola United States of America, United Kingdom le Australia. Sengwalwa se sa nyakišišo se laetša gore melao ye mmalwa yeo e begilwego golaolo gotšewa le gohlakantšha gadikhampani, e hlamilwe ka go fokola, gomme, se se dira gore go be boima goka e kwešiša le go e diriša kamo goswanetšego. Ka ka lebaka leo ge sengwalwa se, se fa ditšhišinyo tša go fetoša le go kagonafatša tše dingwe tša melawana le dinyakwa tša gotšewa le gohlakantšhwa gadikhampani.

Šedi ye tseneletšeng e beilwe go dinyakwa tša kgapeletšo tša gore ge mongdišere wa khamphani a reka goba a hweditše dišere tša go lekana goba go feta dipersente tše masometharo tlhano, a gapeletšwe go reka dišere tšotlhe tše šetšeng tša bengšere ba khamphani, kamo sengwalong se. Sengwalwa se sa nyakišišo se sekaseka le go bapatša dinyakwa tše, tša kgapeletšo, kudukudu ditlamorago tša tšona mo go lekgotlataolo la dikhamphani, le mo tšhomišong ye maleba ya ditshelelete, taolong ye maleba ya dikhampani le gona Matlafatšong ya Bathobaso Ikonoming kamo Afrika Borwa.

Go tšwa dingwalong tša dirutegi, tšeo di fetlekilwego, go laetša gore dinyakwa le melao ye ya kgapeletšo ya bengdišere e thomile go tšwa molatong le sepethong sa *Perlman* gola United States bjalo ka taetšo ya motheo wa gore, bengdišere baswanetše go swarwa ka golekalekana. Go ya ka motheo wo wa menyetla ya go lekalekana, mongdišere yo a nago le kabelo ye kgolo ya khamphani o filwe maatla le tokelo ya pušotaolo ya khamphani. Pušotaolo ye e humile, gomme, moalodi yo moswa o swanetše go ngwathelana lehumo le, le bengdišere ba bangwe nakong ya diphetogo ge molaodi yo moswa a thoma go laola khamphani yeo. Bengdišere ba swanetše go

fiwa monyetla wa go lekalekana gore le bona ba be le kabelo lehumong la khamphani. Ke ka lebaka leo moladi yo moswa a gapeletšwa gore ge goba le diphetogo, molaodi o moswa a tšea taolo ya khampani, a fe bengdišere bao ba šetšego monyetla wa go rekiša dišere tša bona go yena ka tšhelete ye lekanang le ye a e ntšhitšeng go reka taolo ya khampani. Sephetho sa molato wa *Perlman* se tšerwe kua United States of America mo gare ga ngwaga wa 1955.

Sengwalwa se sa nyakišišo se bontšha gore dinyakwa tša kgapeletšo ya bengdišere ka gare ga karolo ya 123 ya Molao wa Dikhampani 71 wa *2008,* ge di lotwa mohlala gore dithomile kae, go ka šupwa molato le sepheto sa *Perlman*. Badiradinyakišišo dibukeng, ba sotše gore moreki wa taolo ya khampani a gapeletšwe go fa bengdišere monyetla wa gore dišere tša bona direkiwe ge a reka taolo ya khampani, go tšwa mahlakoreng a go fapafapana. Go bontšhitšwe gore lebakakgolo ke tšhušumetšo ya sephetho le molato wa *Perlman.* Le ge go le bjalo, go bontšhitšwe gore molato wo le sephetho se, se be se šomišiwa ka baka a maleba feela, mola le mola. Ba bangwe ba dirutegi ba laetša gore sephetho se, ga se sa mafelelo ka gobane diphetho tše tlileng ka morago, di fapane le sepheto se. Le ge go le bjalo, go nale tšhupo ya gore molato yo, e bile seikokotlelo sa go diragatša le go phethagatša motheo wa dinyakwa tša kgapeletšo ya balaodi ba baswa badišere, motheo yoo gobolelwang kudu ka wona mo mererong ya gotšewa le gohlakantšhwa ga dikhampani.

Sengwalwa nyakišišo se ruma ka la gore molao wa dinyakwa tša kgapeletšo ya bengdišere, ga o phethagatšwe Mmušong wa Delaware, gona United States of America. Sengwalwa nyakišišo se, se ruma gape ka la gore kua United Kingdom, molao wo wa dinyakwa tša kgapeletšo go bengdišere ba baswa ke boikokotlelo bja phethagatšo ya menyetla ya go lekalekana gobengdišere ge taolo ya khaphani e fetoga. Eupša taolo le ya dišere gona kua United Kingdom e nabile ka bophara gare ga bengšere ka moo, e kaonafatša ditlamorago tše mpe tša motheo wa taolo ya dikhampani tša naga yeo. Sengwalwa se se gata ka mošito wo tee le mokgwa wo o šomišitšwego ke Australia. Naga ya Australia ga e ena dinyakwa tša kgapeletšo tša bengšere go swana le tšeo di lego karolong ya 123 Molao wa Dikhampani 71 wa *2008*. Melao le taolo ya gotšewa le gohlakantšhwa ga dikhampani ya Australia, e fapana le ya Afrika Borwa. Melao e hlametšwe feela maemo le mebaraka ya Australia. Ke ka lebaka leo sengwalwa se sa nyakišišo, se ruma ka gore dinyakwa tša kgapeletšo tša karolo ya 123 ya Molao wa Dikhampani 71 wa *2008,* ka sebopego sa tšona sa bjale, ga di maleba ka mo Afrika Borwa.

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Chapter 1: Introduction

"[T] he good intentions of the legislature have provided for a form of protection that is costly, unwieldy and unnecessary …"[1]

1 1 Introduction

Globally, takeovers and mergers of companies is big business. Specialist lawyers and accountants practise exclusively in this area of law. Takeovers and mergers are often seen as a method of corporate expansion and diversification. In addition, takeovers and mergers are often used as mechanisms to remove managers who perform poorly. Legal experts and scholars such as Manne[2] have indicated that there is a premise that the market for corporate control is influenced by the performance of managers. If managers perform poorly, the shares of the company would lose value, whereas a sterling performance by managers would increase shareholder value. Hence there is scholarly support for the takeover theory and it has been asserted that a premium is paid in a tender offer because the target's assets will be worth more under management of the bidder than the current management of the target company.[3] The business is not achieving its full potential due to inefficient management.[4]

Researchers refer to takeovers and mergers as a "market for corporate control".[5] These transactions often attract a lot of publicity, both positive and negative. Amongst the reasons for attracting negative publicity, is that bidders are often regarded as "corporate raiders".[6] It is suggested that bidding companies do not create value for shareholders. Other researchers argue that

[1]JR Wiblin "Mandatory takeover offer-too high a price for the economy to pay?" (2004) 29:3 *Journal for Juridical Science* 184.
[2]HG Manne "Mergers and the Market for Corporate Control" (1965) 73:2 *Journal of Political Economy* 111-112.
[3]GR Andre "Tender Offers for Corporate Control: A Critical Analysis and Proposals for Reform" (1987) 2 *Delaware Journal of Corporation Law* 872.
[4]872.
[5]See MC Jensen "Corporate Control and the Politics of Finance" (1991) 4:2 *Journal of Applied Corporate Finance* 13-33.
[6]13.

takeovers and mergers damage morale of target company employees.[7] This in turn, has a negative impact on the productivity of companies and could, consequently, negatively affect a country's economy. It has been indicated that the media often does not notice the activities of such bidders in reducing corporate inefficiencies.[8] Takeovers and mergers remain the most controversial corporate governance mechanism.[9] However, they also play an important role in rendering managers accountable to shareholders.[10] Hostile takeovers are seen as useful instruments for ensuring that management properly administers companies.[11] It is suggested that if there is a threat that a company may be a subject of a takeover if managers do not improve the company's share price performance, managers are encouraged to perform better.[12] Although the debate on the effect of takeovers and mergers on companies' manager performance continues, it is generally asserted that the possibility of acquiring control of a company is necessary for the efficient workings of companies.

Regulation of takeovers and mergers also seeks to uphold some of the objectives and principles outlined by the International Organisation of Securities Commissions, namely: to protect shareholders, to ensure that markets are fair and transparent, and to reduce systemic risk.[13]

This dissertation deals with regulation of takeovers and mergers with a specific emphasis on section 123 of the Companies Act 71 of 2008, (the mandatory

[7]MC Jensen "The Takeover Controversy: Analysis and Evidence" (1986) 4:2 *Midland Corporate Finance Journal* 1.
[8]Jensen (1991) *Journal of Applied Corporate Finance* 13-33.
[9]L Enriques, R Gilson & Pacces A "The Case for an Unbiased Takeover Law (with an Application to the European Union)" (2013) *The Harvard John M. Olin Discussion Paper Series Discussion Paper No. 744, 05/2013*, Available on http://www.law.harvard.edu/programs/olin_center. (Accessed 15 -12- 2015).
[10]JA Armour & DA Skeel Jr "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of US and UK Takeover Regulation" (2007) 95 *Georgetown Law Journal* 1727.
[11]B Rosenzweig "Private Versus Public Regulation: A Comparative Analysis of British and American Takeover Controls" (2007) 18 *Duke Journal of Comparative & International Law* 213.
[12]Armour & Skeel Jr (2007) *Georgetown Law Journal* 1727.
[13]See International Organisation of Securities Commissions "Objectives and Principles of Securities Regulation" (2010) Available at: www.iosco.org/library/pubdocs/pdf/IOSCOD32. Accessed on (20 -3- 2016.)

offer). The mandatory offer is one of the methods of achieving a change of control, and a takeover.

The mandatory offer requirements are set out in section 123 of the Companies Act of 2008.[14] A mandatory offer to other shareholders is required where two types of transactions are concerned: (a) a regulated company reacquires its voting securities in terms of section 48 or in terms of a scheme of arrangement in section 114(1); or (b), a person acting alone has, or two or more related or inter-related persons, or two or more persons acting in concert, have acquired a beneficial interest in voting rights attached to any securities, issued by a regulated company. Furthermore, the mandatory offer will apply to such transactions only where: (a) before that acquisition a person was, or persons acting in concert together, were able to exercise less than the prescribed percentage (currently, 35 percent) of all the voting rights attached to the securities of that company; and (b), as a result of that acquisition, together with any other securities of the company already held by a person or persons who act in concert , and are able to exercise at least the prescribed percentage of all the voting rights attached to the securities of that company.

The mandatory offer as a tool to force a shareholder who acquires control of a company to buy the shares of the remaining shareholders of the company has been a subject of many debates. According to the literature reviewed, it appears that the mandatory offer originates from the 'equal opportunity rule.'[15] As indicated by the court, in the *Perlman case*:

> [T]he rule of equal opportunity would require an offer to buy from minority shareholders."[16]

[14]The Companies Act 71 of 2008 (the Companies Act of 2008.
[15]*Perlman v Feldmann* 219 F 2d 173, 50 ALR 2d 1134, cert. den. 349 US 952 (1955), (Perlman *case).* The case and the equal opportunity rule are discussed in detail in chapter 2 below.
[16]219 F 2d 173, 50 ALR 2d 1134, cert. den. 349 US 952 (1955).

It has been indicated that “The origins of the mandatory offer can be traced to the US *Perlman case*.[17] The mandatory offer rule is only applicable to certain companies that fall under the authority of the Takeover Regulation Panel.[18] The Companies Act of 2008 refers to these companies as “regulated companies” are defined in paragraph 1 8 below. The dissertation undertakes a comparative and critical analysis of the law.

This chapter sets out: the motivation and aim of the research, the research statement, research questions and hypotheses, as well as the research methodology. It also sets the limitation of the research and terminology used. Finally, the chapter provides an outline of the various chapters.

1 2 Motivation and aim of the study

The Guidelines for Corporate Law Reform (the DTI 2004 Policy document),[19] published by the South African Government set out the objectives of government in its company law reform process. The objectives are then set out under section 7 of the Companies Act of 2008. These objectives include: (1) promoting the development of the South African economy, (2) reducing the costs of compliance for companies, (3) encouraging entrepreneurship, (4) encouraging active participation in economic organisations, (5) creating optimum conditions for the aggregation of capital for productive purposes, (6) encouraging the efficient and responsible management of companies, and (7) providing a predictable and effective environment for the efficient regulation of companies.

It appears that many of the objectives of the reform process have not been achieved or have only been achieved partially.[20] The dissertation considers regulation of takeovers and mergers by critically exploring section 123 of the

[17]Katz (1997) *Journal for Juridical Science* 37.
[18] the Takeover Regulation Panel (TRP).
[19]Department of Trade and Industry *South African Company Law for the 21st Century: Guidelines for Corporate Law Reform* (2004) published in GN 1183 in GG 26493 of 23-06-2004.
[20]PJ Sutherland “The State of Company Law in South Africa (A Review of Modern Company Law for a Competitive South African Economy by T Mongalo)” (2012) *Stell* LR 160.

Companies Act of 2008 relating to mandatory offers. It aims to contribute to the practice of company law on takeovers and mergers by analysing the origins of the mandatory offer, problems relating to its implementation, and its impact on the transfer of share ownership. Specific issues about the mandatory offer include: could the mandatory offer rule create entrenched control by managers, and therefore, retard good corporate governance? Does the mandatory offer rule lead to an inefficient use of capital? Could the mandatory offer rule hamper transfer of share ownership, and therefore impede Broad Based Black Economic Empowerment ("BBBEE") transactions? Does the mandatory offer raise costs of undertaking takeovers, and therefore costs for companies? Could the increased costs discourage parties entering into beneficial takeovers? If the answer to these questions is "yes", then it is possible that the mandatory offer rule is working against the objectives set in the DTI 2004 Policy document, as briefly set out above.

Thus, the research deals with reasons why the mandatory offer rule may be inappropriate for South Africa. Other methods of achieving a takeover or a merger will also be discussed with a view to showing how they protect minority shareholders other than the mandatory offer rule. Improvements in takeover and merger provisions brought about by the Companies Act of 2008 will be identified and those provisions that are problematic will be described. The institutions established to regulate takeovers and mergers are reviewed. Finally, conclusions and recommendations will be made as to how to correct any negative impact that the mandatory offer requirements may have.

There is generally a dearth of research on South African takeovers and mergers provisions, particularly as to how they impact on the efforts of the government to promote broad-based ownership of shares, costs of doing business and good corporate governance standards. This dissertation adds to the limited existing body of knowledge in this area of corporate law.

1 3 Research statement

It is an established principle of South African company law that minority shareholders should be protected during a takeover or a merger. The Companies Act of 2008 in part B and C of Chapter 5 and the Companies Regulations 2011, sets out the rules for regulating takeovers and mergers.[21] However, it is argued in this dissertation that while the rationale for regulating other types of takeovers and mergers, such as, the disposal of assets in terms of section 112, the amalgamations or mergers in terms of section 113, the scheme of arrangement in terms of section 114, and the general tender offer in terms of the Companies Act of 2008, are clear and justifiable on various grounds, it is not so easy to establish the rationale for enforcing the mandatory offer rule. Scholars appear to be divided on the policies behind the mandatory offer rule.[22] In this dissertation, it is argued that the bases for the enforcement of the mandatory offer requirement in section 123 of the Companies Act of 2008 are inappropriate for South African financial markets and economy. The mandatory offer rule is one of the most debated aspects in the mergers and takeovers arena.[23] For instance, it has been asked why it is necessary that parties who acquire a specified percentage of a company's shares should grant the same opportunity, and offer the same consideration, to the minority shareholders of the company. The requirement applies even though the price that the acquiring party is required to pay in a mandatory offer has no relation to the market value or underlying value of the shares of the company. The price paid may, for example, be based on a willing-buyer-and-willing-seller basis.

1 4 Research questions

The following research questions will be used to investigate the above statement in respect of mandatory offer requirements.

[21]The provisions will be jointly referred to as the Takeover Provisions in this dissertation.
[22]See among others, MM Katz "Developments in corporate law" *Journal for Juridical Science (*1997) 22(2).39, Wiblin (2004) *Journal for Juridical Science* 184, and L Gullifer & J Payne *Corporate Finance Law Principles and Policy* (2011) 606-616*.*
[23]Wiblin (2004) *Journal for Juridical Science* 3.

1 4 1 What is the rationale for regulating takeovers and mergers in terms of the Companies Act of 2008?

1 4 2 How does Takeover Provisions in South Africa compare to similar rules in other countries?

1 4 3 Are the Takeover Provisions achieving their intended objectives as set out in the Companies Act of 2008?

1 4 4 Are the mandatory offer requirements in terms of section 123 of the Companies Act of 2008 suitable for the South African financial markets and economy and as envisaged by the DTI Policy 2004 document and the Companies Act of 2008?[24]

1 4 5 What conclusions can be reached from the research about the mandatory offer requirements in section 123 of the Companies Act of 2008, and the other methods of achieving a takeover or a merger, and what recommendations can be made to correct any problems identified by the research?

[24]Section 7 of the Act also sets out the intention of the legislature in enacting the new Act. The purposes of this as it relates to profit companies are to:
(a) promote compliance with the Bill of Rights, as provided for in the Constitution, in the application of company law;
(b) promote the development of the South African economy by—(i) encouraging entrepreneurship and enterprise efficiency;
(ii) creating flexibility and simplicity in the formation and maintenance of companies, and
(iii) encouraging transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation;
(c) promote innovation and investment in the South African markets;
(d) reaffirm the concept of the company as a means of achieving economic and social benefits;
(e) continue to provide for the creation and use of companies, in a manner that enhances the economic welfare of South Africa as a partner within the global economy;
(f) promote the development of companies within all sectors of the economy, and encourage active participation in economic organisation, management and productivity;
(g) create optimum conditions for the aggregation of capital for productive purposes, and for the investment of that capital in enterprises and the spreading of economic risk;
(i) balance the rights and obligations of shareholders and directors within companies;
(i) encourage the efficient and responsible management of companies;
(k) provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders, and
(l) provide a predictable and effective environment for the efficient regulation of companies.''

1 5 Hypotheses

In order to investigate, examine and obtain answers to the above questions, the following hypotheses were tested throughout this study:

1 5 1 From time to time financial melt-down has led regulators back to the drawing board as they seek more effective ways of regulating the financial services industry, including mergers and takeovers. In Europe, the integration of European economic markets has brought a sharp focus on policy makers who want to achieve a balance between ownership and control of companies. In addition, policy makers wish to ensure commercial stability as well as socially responsible companies.[25]

1 5 2 The current takeovers and mergers provisions are in some instances unclear and increase the costs of takeovers and mergers.

1 5 3 The mandatory offer requirement in terms of South African company law is inefficient and impede BBBEE and economic transformation of companies.

1 5 4 The mandatory offer rule impedes attainment of the ideals set out in the Companies Act of 2008 of ensuring improved economic development by increasing administration costs and making deal structuring more expensive.

1 5 5 It is necessary to reconsider the application of the mandatory offer rule, taking into consideration the unique economic and financial market conditions in South Africa and the need to promote BBBEE; promote corporate governance; encourage efficient use of capital; and promote the objective set in the Companies Act of 2008.

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[25] CM Rafferty "*The "means and ends" of regulating barriers to takeover bids: How effectively will the European Takeovers Directive 2004 control defensive measures in hostile takeovers?* Thesis presented for the Degree of Master of European Studies Academic Year 2005-2006. Course: European Company Law. College of Europe. Brugge Campus. (2006) 3.

1 5 6 The takeover and merger requirements in the Companies Act of 2008 are sufficient to deal effectively and efficiently with protection of shareholders. However, it is necessary to improve and clarify some provisions.

1 6 Methodology

1 6 1 Literature Review

In order to answer the various research questions for this study, a literature review on takeovers and mergers provisions of various countries with particular reference to the mandatory offer has been undertaken. A comparative critical analysis of the various takeover and merger procedures is undertaken.

1 6 2 Countries covered in the research

The dissertation comparatively considers regulation of takeovers and mergers, focusing on the mandatory offer in selected countries, including South Africa. The rationale for adopting the mandatory offer requirement in those countries, if any, are analysed and discussed in order to understand why they adopted this requirement. The reasons and experiences on why and how the mandatory offer requirement is applied will be useful for South Africa. Academics have pointed out that:

> "It is not only important to understand the company laws of other countries in those areas where we have borrowed from them but it is also necessary that we comprehend why we have sometimes followed our own course or why we have adopted rules from one jurisdiction rather than another.''[26]

[26]Sutherland (2012) *Stell* LR 159.

The comparative discussion will include the company laws of the United States of America - Delaware State, United Kingdom and Australia. These three jurisdictions have been chosen for the following reasons:

1 6 2 1 United States of America- The State of Delaware

The United States of America (US) and, specifically the State of Delaware, has been chosen as a comparative jurisdiction on the basis that the Companies Act of 2008 has introduced a number of US company law provisions, including those specifically intended for greater protection of shareholders during takeovers and mergers.[27] The State of Delaware has been a preferred state for incorporation of major companies for a number of years and this is still the position today.[28] It has more developed and sophisticated corporate law precedents due to the expertise of its judges.[29] Therefore, it may be useful to examine how the rules relating to protection of minority shareholders operate, particularly in the absence of the mandatory offer bid as the State of Delaware does not apply the mandatory offer requirement.

1 6 2 2 The United Kingdom

The United Kingdom (UK) has been selected because South African takeovers and mergers regulations are mainly based on the UK's City Code on Takeovers and Mergers.[30] The UK's takeovers and mergers regulations are commonly referred to as the "City Code".[31] The UK City Code has been amended

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[27]N Boardman "A critical analysis of the new South African takeover laws as proposed under the Companies Act 71 of 2008" (2010) *Acta Juridica* 313. See also section 164 of Companies Act 71 of 2008 dealing with appraisal rights and section 113 dealing with amalgamations and mergers.

[28]WJ. Carney, GB. Shepherd, & J Shepherd Bailey "Lawyers Ignorance, and the Dominance of Delaware Corporate Law" (2012) Vol.2 *Harvard Business Law Review* 123.

[29]DA Oesterle *The Law of Mergers and Acquisitions* (2005) 31.

[30]See the explanatory note to the Securities Regulation Code and the Rules of the Securities Regulation Panel. Government Gazette12962. January 1991. The Securities Regulation Code and the Rules of the Securities Regulation Panel forms the basis of the current Takeover Provisions. See the DTI 2004 Policy document, where it is indicated that the current rules administered by the Securities Regulation Panel will be maintained.

[31]See B Clarke "Reinforcing the Market for Corporate Control" (2010) UCD Working Papers in Law, Criminology & Sociology-Legal Studies Research Paper No 39/2010. 9. Available at SSRN: http://ssrn.comabstract=1661620. (Accessed 20-05- 2016).

significantly in order to meet the requirements of the European Union Takeover Directive (EU Directive)[32] and the discussions will incorporate some comments about the EU Directive to broaden the understanding of the mandatory offer requirements. It was considered useful to examine how UK takeover and merger regulators apply and enforce the mandatory offer requirement. As Yeats points out, any research that does not include jurisdictions from which concepts have been sourced would be incomplete and lacking academic depth.[33]

1 6 2 3 Australia

Finally, Australia has been selected as a comparative jurisdiction on the basis that, like South Africa, the origin of its company law is the UK. However, its takeovers and mergers provisions are somewhat different, even though they share some elements with those of the UK. There are distinct differences in takeover and merger regulation between the UK and Australia. An exploration of the different regulations will be useful for SA in assessing its regulations.

1 7 Limitations of the scope of the research

Takeovers and mergers involve many aspects of company law and may include other areas of the law such as, labour law or public interest law or competition law. This research does not deal with those issues, but it is solely concerned with the laws, authorities and regulations aimed at protecting shareholder interests during a takeover or a merger.

The dissertation covers the current law under the Companies Act of 2008. It does not discuss the possible amendments under the Draft Companies

[32]Directive 2004/25 EC of the European Parliament and of the Council European of 21 April 2004 on takeover bids, Official Journal of the European Union, 30.4.2004.

[33]J Yeats *The Effective and Proper Exercise of Appraisal Rights Under the South African Companies Act, 2008: Developing a strategic approach through a study of comparable foreign law,* A thesis presented for the degree of Doctor of Philosophy Commercial Law Department, University of Cape Town. (2015) 40.

Amendment Bill.[34] These amendments were published during the final stages of completing this thesis and they accordingly could not be accommodated.

1 8 Terminology

Over the years, takeovers and mergers practitioners have developed their own jargon. In this section, a number of terms are defined that are used throughout the dissertation.

1 8 1 An **"affected transaction''** [35] is the umbrella term used to describe all the different types of takeovers and mergers. Blackman et al indicate that the meaning of the term 'affected transaction' is very broad.[36]

1 8 2 **"takeover"** is often used instead of "acquisition.[37] The term "takeover" is not a "term of art".[38] A takeover refers to a transaction whereby a person indirectly acquires control over the assets of a company by acquiring control of the management of a company, usually by acquiring a significant shareholding in that company. The existence of a company

[34] The dti has published a Draft Companies Amendment Bill in Government Gazette 41913, for public comments. Members of the public have been invited to submit comments by 23 November 2018. Available at: https://pmg.org.za/call-for-comment/740/.Accessed 5 -11-2018.
[35] Section 117(1) (c) of the Companies Act of 2008 defines affected transactions as:
"(i) a transaction or series of transactions amounting to the disposal of all or the greater part of the assets or undertaking of a regulated company, as contemplated in section 112, subject to section 118(3);
(ii) an amalgamation or merger, as contemplated in section 113, if it involves at least one regulated company, subject to section 118(3);[35]
(iii) a scheme of arrangement between a regulated company and its shareholders, as contemplated in section 114, subject to section 118(3);
(iv) the acquisition of, or announced intention to acquire, a beneficial interest in any voting securities of a regulated company to the extent and in the circumstances contemplated in section 122(1);
(v) the announced intention to acquire a beneficial interest in the remaining voting securities of a regulated company not already held by a person or persons acting in concert;
(vi) a mandatory offer contemplated in section 123; or
(vii) compulsory acquisition contemplated in section 124."
[36] MS Blackman, RD Jooste & GK Everingham *Commentary on the Companies Act* Volume 1 (2002) 18.
[37] See JT Pretorius, PA Delport, M Havenga & M Vermaas Hahlo's *South African Company Law through cases: A source book* (1999), 569, in which the word is generally used to denote affected transactions as defined in Chapter XVA of the Companies Act of 1973 and the SRP Code.
[38] Blackman *et al Commentary on the Companies Act* Volume 3. 18-9.

is not affected and it rather implies merely a change in the main shareholders or the introduction of a new substantial shareholder.[39] The acquisition of control of a company may also be achieved by controlling the majority votes of the directors of the target.[40] Another method of achieving a takeover is for the bidder to purchase the assets or business of the target.[41]

1 8 3 The Companies Act of 2008 does not specifically define what **"control"** for the purposes of affected transactions is. The control referred to in section 2 of the Companies Act of 2008 relates to what is often referred to as *de facto* control or statutory control, being a holding of over 50 percent of the shares.[42] However, for the purposes of affected

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[39]HS Cilliers, ML Benade, JJ Henning, JJ Du Plessis & PA Delport *Corporate Law* 2 ed (1992) 457.

[40]L Bebchuk & O Hart. "Takeover Bids vs. Proxy Fights in contests for corporate control." Discussion Paper No. 336. 10/2001*. Harvard Law School Cambridge, MA 02138*. *The Center for Law, Economics, and Business*. Available at: http://www.law.harvard.edu/programs/olin_center/> (Accessed 20-1-2011). See also the definition of control referred to in chapter 1, paragraph 1 8 above.

[41]Section 112 of the Companies Act of 2008.

[42]Section 2 of the Companies Act of 2008 indicates control as:
(1) For all purposes of this Act—
(*a*) an individual is related to another individual if they—
(i) are married, or live together in a relationship similar to a marriage; or
(ii) are separated by no more than two degrees of natural or adopted consanguinity or affinity;
(*b*) an individual is related to a juristic person if the individual directly or indirectly controls the juristic person, as determined in accordance with subsection (2); and
(*c*) a juristic person is related to another juristic person if—
(i) either of them directly or indirectly controls the other, or the business of the other, as determined in accordance with subsection (2);
(ii) either is a subsidiary of the other; or
(iii) a person directly or indirectly controls each of them, or the business of each of them, as determined in accordance with subsection (2).
(2) For the purpose of subsection (1), a person controls a juristic person, or its business, if—
(*a*) in the case of a juristic person that is a company—
(i) that juristic person is a subsidiary of that first person, as determined in accordance with section 3(1) (*a*); or
(ii) that first person together with any related or inter-related person, is—
(*aa*) directly or indirectly able to exercise or control the exercise of a majority of the voting rights associated with securities of that company, whether pursuant to a shareholder agreement or otherwise; or
(*bb*) has the right to appoint or elect, or control the appointment or election of, directors of that company who control a majority of the votes at a meeting of the board;
(*b*) in the case of a juristic person that is a close corporation, that first person owns the majority of the members' interest, or controls directly, or has the right to control, the majority of members' votes in the close corporation;

transactions, control is defined with reference to the specified percentage as indicated for a mandatory offer in terms of section 123 of the Companies Act of 2008. It is the holding of 35 percent or more of the voting securities of a company.

Regulation 81(e) of the Takeover Regulations defines '**control'** as:

> "[T] he holding of a beneficial interest in a regulated company equal to or exceeding the specified percentage of voting rights in that regulated company."

The various definitions of control are not consistent. It has been suggested that the definitions should be amended for clarity.[43]

1 8 4 **"Regulated company"** is defined in section 117(1) (i) as: a company to which this Part, Part C and the Takeover Regulations apply, as determined in accordance with section 118(1) and (2).[44]

(*c*) in the case of a juristic person that is a trust, that first person has the ability to control the majority of the votes of the trustees or to appoint the majority of the trustees, or to appoint or change the majority of the beneficiaries of the trust; or
(*d*) that first person has the ability to materially influence the policy of the juristic person in a manner comparable to a person who, in ordinary commercial practice, would be able to exercise an element of control referred to in paragraph (*a*), (*b*) or (*c*).

[43]S Luiz "Some comments on the scheme of arrangement as an "Affected Transaction" as defined in the C*ompanies Act* 71 of 2008" (2012) *PER* 15 (5) Available on http://dx.doi.org/10.4314/pelj.v15i5.4, (Accessed 20-7-2013).

[44]Section 118(1) provides that: subject to subsection (2) to (4), this Part, Part C and the Takeover Regulations apply with respect to an affected transaction or offer involving a profit company or its securities if the company is:
"(a) a public company;
(b) a state-owned company, except to the extent that any such company has been exempted in terms of section 9; or
(c) a private company, but only if—
(i) 10 percent or more of the issued securities of that company that have been transferred, other than by transfer between or among related or interrelated persons, within the period of 24 months immediately before the date of a particular affected transaction or offer exceeds the percentage prescribed in terms of subsection (2); or
(ii) the Memorandum of Incorporation of that company expressly provides that the company and its securities are subject to this Part, Part C and the Takeover Regulations, irrespective of whether the company falls within the criteria set out in subparagraph (i)." Section 118(2) provides:"The Minister, after consulting the Panel, may prescribe a minimum percentage, being not less than 10%, of the issued securities of a private company which, if transferred within a 24-month period as contemplated

1 8 5 In this dissertation, the following terms are used interchangeably: "takeovers and mergers" and "affected transactions";[45] "offeree" and "target";[46] "offeror" and "bidder";[47] and; "offeree shareholders" and "target shareholders."

1 9 Content and arrangement of chapters

Chapter 1 Introduction

This chapter provides the background for the research, sets out the motivation and aims of the research, provides the research statement, research questions and hypotheses, discusses the methodology adopted in the research, indicates countries selected for the research and gives brief reasons why they were chosen, and sets out the scope of the research. Finally, it provides an outline of the discussions in the various chapters.

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in subsection (1) (*c*) (i), would bring that company and its securities within the application of this Part, Part C, and the Takeover Regulations in terms of that subsection."
Section 118(3) indicates that:
"Despite the definition of „affected transaction" set out in section 117(1) (*c*), this Part, Part C and the Takeover Regulations do not apply to—
(*a*) a proposal to dispose, or disposal, of all or the greater part of the assets or undertaking of a regulated company;
(*b*) a proposed amalgamation or merger involving at least one regulated company; or
(*c*) a scheme of arrangement proposed by a regulated company, to the extent that any such affected transaction is pursuant to or contemplated in an approved business rescue plan in terms of Chapter 6."
Section 118(4) provides:
"(4) If there is a conflict between any provision of this Part, Part C, or the Takeover Regulations, and any provision of another public regulation—
(*a*) the conflicting provisions apply concurrently to the extent that it is possible to apply and comply with one of the inconsistent provisions without contravening the second; and
(*b*) to the extent that it is impossible to apply or comply with one of the inconsistent provisions without contravening the second, the provisions of the other public regulation prevail."
[45]The phrases are used for convenience depending on the context.
[46]For purposes of takeovers and mergers, the UK City Code and the SA Takeover Regulations use "offeree" while the Australian Corporations 2001 Act uses "target".
[47]For purposes of takeovers and mergers, the UK City Code and the SA Takeover Regulations use "offeror", while the Australian Corporations 2001 Act uses "bidder".

Chapter 2 An overview of the regulation of takeovers and mergers in the United States of America – the State of Delaware

In this chapter, regulation of takeovers and mergers in the US State of Delaware is discussed as the US does not have a single takeover law. The State of Delaware was chosen because large companies prefer it as their state of incorporation. The origin of the equal opportunity rule is discussed with a view to understanding how it developed into the mandatory offer requirement. The chapter further provides an overview of the various standards of reviewing conduct of directors including the Business Judgment Rule (BJR), and how the courts apply the standards to the conduct of directors during takeovers and mergers. The appraisal right in section 164 of the South African Companies Act of 2008 originates in the US and, therefore, it is appropriate that the appraisal right be discussed to understand how it is applied in the State of Delaware.

Chapter 3 An overview of the application of mandatory offer requirement in the United Kingdom

The development of English company law on regulation of takeovers and mergers is discussed, with particular reference to the mandatory offer rule. The reasons for the development of the rule are explored. Observations are made as to how the mandatory offer rule is applied in the UK compared to South Africa. The regulatory body enforcing the mandatory offer rule and their processes are discussed. The discussions also cover the criticism and the debates relating to the mandatory offer rule.

Chapter 4 An overview of the regulation of takeovers and mergers in Australia

This chapter deals with Australian company law relating to takeovers and mergers. Even though Australian company law originates from English company law, takeover and merger regulations are different. The dissertation discusses some of the reasons why Australian takeover and merger rules deviates from the UK mandatory offer. The chapter considers the different regulatory bodies and their procedures.

Chapter 5 An overview of the regulation of takeovers and mergers in South Africa with specific emphasis on the mandatory offer

In this chapter, South African takeover law is discussed with specific emphasis on the application of the mandatory offer rule. The reasons for the development of the mandatory offer rule is discussed and critiqued. In addition, other methods of achieving a takeover or a merger are discussed. These methods include proposals to dispose of all or the greater part of the assets or undertaking of a company_in terms of section 112 of the Companies Act of 2008, amalgamations and mergers in terms of section 113 of the Companies Act of 2008, the scheme of arrangement in terms of section 114 of the Companies Act of 2008 and the general tender offer, followed by the compulsory acquisition in terms of section 124 of the Companies Act of 2008. In addition, any shortcomings of South Africa’s mandatory offer requirement under section 123 of the Companies Act of 2008 are identified.

The relevant case law is examined and integrated throughout the discussion. The few cases dealing with the protection of minority shareholders during takeovers and mergers are analysed and critiqued.

Chapter 6 Evaluating takeover and merger provisions of selected countries

This chapter evaluates the different regulatory regimes in respect of takeovers and mergers applied by different countries. In particular, a comparison is made in respect of: development of takeover and merger regulations and the reasons for such regulations; the types of takeovers and mergers regulated and reasons for such divergence; the authorities and statutes for regulating takeovers and mergers and the reasons for difference; dispute resolution methods for takeovers and mergers; enforcement measures for takeovers and mergers and an evaluation of arguments for and against the mandatory offer requirement. The origin of the mandatory offer is questioned and the application of the rule is also critiqued. Furthermore, the problems relating to the application of the mandatory offer in the context of South Africa are identified. The differences and similarities between the legislation of the comparative countries are highlighted.

Chapter 7 Conclusions and recommendations

This final chapter discusses the findings of the research. Based on these findings, the chapter also provides a number of recommendations for improvement of takeover and merger provisions in South Africa. These recommendations are aimed at creating regulatory solutions that suit local economic conditions. It is suggested that some of the takeover provisions be amended to promote efficiency and certainty in the regulation of takeovers and mergers. In addition, recommendations are made that some takeovers and mergers provisions that have been found wanting, be amended. Of particular importance is a practical suggestion for the amendment of section 123 of the Companies Act of 2008 with a view to promoting good governance, facilitating BBBEE transactions, and promote efficient usage of capital as envisaged in the Companies Act of 2008.

Chapter 2: An overview of the regulation of takeovers and mergers in the United States of America-The State of Delaware

"Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred."[1]

2 1 Introduction

The purpose of this chapter is to provide an overview of regulation of takeovers and mergers in the US with specific reference to the State of Delaware. A number of provisions of the SA Companies Act of 2008 are based on the company laws of other countries, and it is therefore reasonable to make comparisons as to how these laws operate in their country of origin. A number of sections of the Companies Act of 2008 have been adopted primarily from the US and Canada.[2] These include: section 66(1) relating to the allocation of powers to manage the company to the directors; section 76(4) - the business judgment rule;[3] section 113 in respect of amalgamations or mergers;[4] and section 164 in respect of appraisal rights. It is difficult to undertake a comparative analysis of the law of different countries in general.[5] This is particularly relevant when comparing the US and South African law due to a

[1]*Unocal Corp v Mesa Petroleum Corp* 493 A.2d 948, 954 (Del 1985).

[2]J Latsky "The fundamental transactions under the Companies Act: A report back from practice after the first few years" (2014) *Stell LR 2* 372.

[3]FHI Cassim "The Duties and the Liability of Directors" in Cassim (Man Ed) *Contemporary Company Law* (2012) 563. Cassim indicates that the rule applied in the USA for over 160 years and is regarded as cornerstone of corporate law.

[4]See FHI Cassim "Introduction to the New Companies Act: General Overview of the Act" in Cassim (Man Ed) *Contemporary Company Law* (2012) 16, where it is indicated that section 113 is modelled on Delaware General Corporations Law.

[5]*CM* Bruner *"*Power and Purpose in the "Anglo-American" Corporation" (2010) 50:3 *Virginia Journal of International Law* 589. In this article, Bruner refers to *The Anatomy of Corporate Law* - a book reflecting "collaboration among nine authors from six countries, and points out that "It has been aptly said, "no model is better than its assumptions." The validity and utility of conclusions drawn from such comparative studies, then, will depend critically on accurate identification of a true common problem, and this determination is where functionalism encounters a substantial challenge."

number of factors, including that the US has a federal system of government. In the US, state laws and federal laws often operate side by side, while in South Africa there is only one company law regime. There are also considerable differences on how states regulate corporations.[6] It is indicated that in some instances the line between state laws and federal law is blurred.[7] Corporate law is primarily the domain of the states, resulting in 50 different state laws.[8] There is no single corporate national law in the US and takeover law is positioned on the interface of company law and securities regulation.[9] This is contrary to the other comparative countries where securities laws and company laws are clearly separated. There is also no unitary takeover law in the US and there are no mandatory offer rules, although no state is precluded from enacting such a law.[10] A view is taken here that a comparative analysis of the US corporate law is too broad. Accordingly, the analysis will be mainly restricted to the regulation of takeovers and mergers in the State of Delaware.

2 2 An overview: The equal opportunity rule in takeovers and mergers

The equal opportunity rule appears to form a basis for the mandatory offer requirement in South Africa, which requirement was originally in the SRP Code.[11] The mandatory offer requirement is now in section 123 of the Companies Act of 2008. The equal opportunity rule seeks to give all shareholders of the company an opportunity to sell their shares at the same price and on the same terms when a change of control of a company occurs. The price and terms must be based on those of the controlling shareholder when it sold its shares to the new controlling shareholder.[12] The new controller

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[6]K Van der Linde *Aspects of the regulation of share capital and distributions to shareholder* LLD thesis UNISA (2008) 59.
[7]EP Schuster "Efficiency in Private Sales -The Case for Mandatory Offer Bids" (2010) *LSE Law, Society and Economy Working Papers 08/2010 London School of Economics and Political Science* 9.
[8]9.
[9]9.
[10]9.
[11]See MM Katz "Developments in corporate law" (1997) 22:2 *Journal for Juridical Science* 39. See also Schuster (2010) *LSE Law* 3.
[12]WD Andrews "The Stockholder's right to equal opportunity in the sale of shares" (1965) 78: 3 *Harvard Law Review* 515-516.

has an obligation to the remaining shareholders and must then fulfill it before it assumes control of the company.[13]

Private sale of corporate control is regarded as controversial. Some of the debates are focused on whether it is legitimate for a controlling shareholder to exclusively appropriate the control premium paid by a buyer.[14] The question asked is whether controlling shareholders must share in the 'premium of control'. There are three main theories about the premium of control, namely:

> "(a) That it is a corporate asset – a theory devised by Professors Berle and Means;
> (b) That it should be equally shared among shareholders – the so-called 'equal sharing rule,' proposed by Professor Andrews; and
> (c) That the law regarding these premiums should be deregulated (supported by law and economics scholars)."[15]

Change of corporate control transactions can raise complex matters,[16] and the debates on the payment of a premium for control during the sale of corporate control have also produced numerous academic articles.[17] In the US, early opinions on payment of a control premium have given way to modern rules: the majority shareholder does not owe minority shareholders any duty when selling control.[18] Early commentary indicates that there were a number of concerns about the development of the rule for sharing of a premium of control. It was felt that this would negatively restrict the ability of controlling shareholders to sell their shares. Researchers and academics have also pointed out that case law relating to the payment of a premium for control to the controller did not aid

[13]Andrews (1965) 78: 3 *Harvard Law Review* 515-516.
[14]SM Sepe "Private Sale of Corporate Control: Why the European Mandatory Offer Bid Rule is Inefficient" (2010) *Arizona Legal Studies Discussion Paper* 10-29, 15. Available at: SSRN: https://ssrn.com/abstract=1086321.
[15]15.
[16]RW Jennings "Trading in Corporate Control" (1956) 1 *California Law Review* 1.
[17]A Berle "The Price of Power: Sale of Corporate Control" (1965) 50 *Cornell Law Quarterly* 629.
[18]FH Easterbrook & DR Fischel "Corporate Control Transactions" (1982) 91 *The Yale Law Journal* 698.

the interpretation of the law.[19] It has been asserted that the theories relating to payment of a control premium are inconsistent and resulted in confusing precedent.[20] Against this background, *Perlman v Feldmann,*[21] a decision of the United States Court of Appeals for the Second Circuit emerged. The debates on corporate control were brought into greater focus by the *Perlman* case.[22] The decision of the court is often viewed as controversial.[23] It is asserted that *Perlman case* is one of the most widely-discussed cases, and yet few lawyers understand its meaning.[24] *Perlman* raised the issue whether a controlling shareholder who sells a controlling block of shares to outsiders at a price, which is not available to all shareholders, is compelled to pay over to the company, or to other shareholders any premium that exceeds the investment value of the shares.[25]

The facts of the *Perlman case* are briefly as follows: During the Korean War, there was a shortage of steel, which increased the price of steel. Newport Steel Corporation (Newport), and some US companies could maintain stable steel prices and allocated steel to various companies. This created a shortage which meant that steel users found it difficult to obtain steel.[26] Feldmann was the controller of Newport and realised an opportunity to sell his controlling stake to Wilport Company (Wilport) at a profit. Wilport represented a group of steel users. It desired to obtain control over the selection of Newport clients.[27] to ensure and protect steel supplies to the group.[28] Feldmann, resigned his seat on the board of Newport, together with his fellow directors, thereby handing over control to Wilport. The controlling stake was sold at a substantial premium over the market price. Perlman, one of the minority shareholders, sued and

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[19]Duke L.J. "The Sale of Corporate Control at a Premium: An Analysis and Suggested Approach" (1961) *Duke Law Journal* 554.
[20]Duke L.J. (1961) *Duke Law Journal* 554.
[21]219 F.2d 173 (2d Cir 1955).
[22]Jennings (1956) *California Law Review* 1.
[23]Duke (1961) *Duke Law Journal* 554, 557.
[24]JG Deutsch "Perlman v Feldmann: A Case Study in Contemporary Corporate Legal History" (1974) 8 *Journal of Law Reform* 7.
[25]Jennings (1956) *California Law Review* 1.
[26]Easterbrook & Fischel (1982) *The Yale Law Journal* 717.
[27]WN Snell "Reflections on The Practical Aspects Of "The Sale of Corporate Control" (1972) *Duke Law Journal* 1200.
[28]1200.

claimed that the sale was not a sale of shares but involved an unlawful sale of corporate control. It was argued that Feldmann, as director and controller, had a fiduciary duty to the company and other shareholders. Based on this argument, Feldmann should not appropriate the premium paid for control. Feldmann argued that it was merely a sale of a controlling stake, which stake has attached to it rights, powers and advantages.[29] The district court ruled in favour of Feldmann, but on appeal, the appeal court gave judgment in favour of Perlman, and referred the matter back to the district court to determine the final purchase price to be allocated to the control premium. According to the court ruling, once the premium was established, it had to be shared pro rata between the plaintiffs to the extent of their shareholdings.[30]

The Perlman case did not settle "this confused area of the law"[31] and later judicial pronouncements did not favour the sharing of the control premium.[32] Although it is acknowledged that transfer of corporate control can be abused, scholars assert that it must be approached analytically on a case-by-case basis.[33] There are adequate corporate rules to prevent possible abuse.[34] The sale of control at a premium could be an advantage for remaining shareholders, as the new controller has an incentive to operate the company for the benefit of all. It is argued that the prohibition of sale at a premium has the effect of restricting free transfer of the sale of corporate control - contrary to sound economic policy.[35] Majority shareholders are able to sell the stock at a premium "precisely because it carried control power with it."[36]

In certain circumstances, it may be difficult to determine the circumstances under which minority shareholders must be afforded an equal opportunity to share in the premium of corporate control. These include when corporate

[29]Jennings (1956) *California Law Review* 2-4.
[30]4-5.
[31]Duke (1961) *Duke Law Journal* 560.
[32]558-560.
[33]560-566.
[34]566.
[35]See Duke (1961) *Duke Law Journal* 565-566.
[36]Berle (1965) Cornell Law Quarterly 628.

control is transferred by means of a sale of a minority shareholding that has the ability to influence the board. A minor shareholding has the ability to vote the majority of the board. This occurs where there is wide spread shareholding, inactive shareholders or shareholders have come to rely on management.[37] Sharing of a premium may restrain transactions at huge cost to parties who would otherwise want to conclude such transactions. Corporate law is aimed at maximising profits and, unlike in the political arena, equality of treatment is "not justified for its own sake."[38] Other scholars have commented that "*Perlman v. Feldmann* was an aberration arising out of a failure of the pricing system to allocate resources."[39] Bainbridge[40] comments that the *Perlman case* is more than just controversial. He further states:

> "It is an outlier. The overwhelming weight of authority confirms that a controlling shareholder is free to sell at any price he or she gets, without having to share the premium with the minority or providing an alternative exit for the minority, absent usurpation of a corporate opportunity or sale to a looter."[41]

Letts states that:

> "A blanket rule prohibiting the retention by the seller of any premium paid for control, or requiring equal opportunity for other shareholders, makes sense only upon the assumption either that all shareholders should always be equal with respect to sales of their shares, or that some evil is prevented which cannot properly be prevented in some other way."[42]

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[37]See 633-634. In these paragraphs, Berle list the difficulties of sale of control. He points to incidences where the sale price for the shares incorporate the influence the seller has on old directors as well as the actual shares. In this scenario, the sale of the shares also includes the relationship the seller had with the directors.
[38]JB Javaras "The Equal Opportunity in the Sale of Controlling Shares: A Reply to Professor Andrews" (1965) 32 *University of Chicago Law Review* 428.
[39]B Manning "Shareholder's Remedy An Essay for Frank Coker" (1962) 72 *The Yale Law Journal* 223 - 225.
[40]See S Bainbridge "There is No Affirmative Action for Minorities, Shareholder and Otherwise, in Corporate Law" (2008) 118 *Yale LJ Pocket Part* 71.
[41]Bainbridge (2008) *Yale LJ Pocket Part* 71, 74.
[41]JS Letts "Sales of Control Stock and the Rights of Minority Shareholders" (1970-1971) 26 *Bus Law* 631 637.
[41]646.
[42]Letts (1970-1971) *26 Bus Law* 631 637.

The equal opportunity rule is designed to deal with issues of looting and corporate squeeze. The problems result from abuse of the control position. The abuse can occur at any time and does not require any transfer of control.[43] In his discussion of the *Perlman case,* Deutsch indicates:

> "As a lawyer who practiced corporate law in the middle 1960's, I can testify that at least some of the corporate bar viewed *Perlman v. Feldmann* as a "drastic departure from the existing law regarding stock ownership … [creating] a federal rule at variance with corporate laws of the several states.''[44]

The requirement for a premium to be paid as an "anti-dote" for looting is like banning an investment in shares in order to avoid bankruptcy.[45] It is not correct to suspect that all acquirers of companies have the intention of looting and it is asserted that unequal distribution of gains from corporate control transactions eventually promote the interests of shareholders.[46]

Easterbrook and Fischel,[47] indicates that in the US,

> "[T] he mountain of academic commentary calling for some type of sharing requirement has not been influential, and the legal treatment of control sales is largely along the lines of wealth maximising. Sales at a premium are lawful, and the controlling shareholders generally have no duty to spread the bounty."

As can be seen from the commentaries above, the introduction of the equal opportunity rule concerned a number of scholars. However, the rule did not become law in the years since the *Perlman case* was decided.[48] American courts appear not to be influenced much by the several academic theories formulated around private sales of corporate control.

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[43] 646.
[44] JG Deutsch "Perlman v Feldmann: A Case Study in Contemporary Corporate Legal History" (1974) 8 *Journal of Law Reform*. 44
[45] See Easterbrook & Fischel (1982) *The Yale Law Journal* 718.
[46] 736.
[47] 716.
[48] Deutsch (1974) *Journal of Law Reform* 45.

In the State of Delaware, it is settled law that controlling shareholders do not have to share a control premium with non-controlling shareholders. The rationale for the courts is that in making decisions on corporate control, the courts should not interfere in arm's-length commercial transactions. The courts follow a hands-off approach: unless there is clear and visible harm done, there is no reason to require than an equal opportunity be given to other shareholders in private sales of control. The rule was formulated in *Zetlin v Hanson Holdings Inc*.[49] The court in this matter recognised that those who invest their capital necessary to acquire a major shareholding and ownership of a corporation have the right to control the company.[50] The decision in *Zetlin case* was very short (one page).[51] The facts were briefly, Zetlin held 2 percent shares in Gable Industries, Inc. (Gable). Hanson Holdings, Inc., Sylvestri, and other family members held 44.4 percent of Gable's shares. Hanson and others sold their 44,4 percent shareholding to a new controlling shareholder, Flintkote Co, at a premium price of $15 per share, while the shares were trading on the stock market at $7.38 per share. It was accepted by all parties that the sale of the 44.4 percent to Flintkote Co effectively transferred control of Gable Industries Inc. to Flinkkote Co. Having lost the case on a first round, Zetlin appealed, and the Court of Appeals indicated that those who invest the capital necessary to acquire a dominant position in the ownership of a corporation have the right of controlling that corporation. The court also indicated that, "it has long been settled law that, absent looting of corporate assets, conversion of a corporate opportunity, fraud or other acts of bad faith, a controlling stockholder is free to sell, and a purchaser is free to buy, that controlling interest at a premium price." The court pointed out that while,

> "[M]inority shareholders are entitled to protection against such abuse by controlling shareholders. They are not entitled, however, to inhibit the legitimate interests of the other stockholders. It is for this reason that control shares usually command a premium price. The premium is the added amount an investor is willing to pay for the privilege of directly influencing the corporation's

[49]See 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York**.**
[50]Sepe 2010 *Arizona Legal Studies Discussion Paper*18; and *Schuster* 2010 *LSE Law* 11-12.
[51]See 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York**.**

affairs."

The court then rejected the contention of Zetlin that minority stockholders are entitled to an opportunity to share equally in any premium paid for a controlling interest in the corporation.[52] The court indicated that the requirement would deeply affect the manner in which controlling shares are transferred.[53] This would require that a controlling stake must be transferred only by means of an offer to all shareholders.[54] The court indicated that the requirement would be contrary to existing law.[55]

The market rule approach, also called the 'private negotiation rule',[56] is one of the methods to acquire control of a company. It has been defined in the literature as a framework that:

> "(i) allows the incumbent controller to sell his shares together with the effective control over the company at any price he is able to achieve, without having to share the proceeds with his fellow shareholders (and/or the company);
> (ii) does not require the acquirer of the shares to offer to the remaining shareholders to buy the residual shares; and
> (iii) allows the acquirer to voluntarily make an offer for the residual shares, at any price he thinks fit, without any reference to the price he paid to the (former) block holder."[57]

2 3 An overview: Statutes and authorities applicable in takeovers and mergers

2 3 1 The Delaware General Corporations Law and the Delaware courts

Delaware General Corporations Law (DGCL) regulates most US large public corporations, as indicated in chapter 1. Van der Linde states that the state of

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[52] 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York.
[53] 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York.
[54] 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York.
[55] 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York.
[56] Schuster (2010) *LSE Law* 9.
[57] 13.

Delaware "has a reputation as the most permissive, and consequently also the most popular, state for incorporations in America."[58] The DGCL sets out a division of powers between the directors and shareholders. The DGCL provides in section 141(a) the broad principle that: "the business and affairs of every corporation … shall be managed by or under the direction of a board of directors." [59] This section is often used to support actions taken by directors against any challenges by shareholders. The section supports the application of the BJR.[60]

Under the DGCL, majority shareholders cannot directly compel the board to take any particular action, and it is suggested that in the charters of incorporations, shareholders cannot be given the power to do so.[61] In the State of Delaware, a director-centred approach is followed towards takeovers and mergers, which gives discretion to the directors to decide on the outcome of a takeover.[62] An alternative to this is the director-and-shareholder approach where the directors decide to enter into a corporate control transaction and the shareholders participate by voting. American corporate law supports this bilateral approach in instances where agency problems exist and the consequent conflict of interests, particularly where directors are in the final stage of their tenure, such as in transactions involving a change of control.[63] Delaware's state law gives generous leeway to directors in the management of corporations. It has the most flexible provisions on mergers and takeovers in the US and there is evidence that in some instances, companies relocate their place of incorporation to this state a few hours before a major acquisition, in order to benefit from its flexible takeover and merger provisions.[64]

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[58]K Van der Linde "The regulation of share capital and shareholder contributions in the Companies Bill 2008" (2009) 1 *TSAR* 42.
[59]DGCL section 141(a).
[60]See detailed discussions under paragraph 2 5 3 on the BJR. The BJR is seen as the corollary of the common law principle that directors manage the affairs of a corporation. See RJ Holland "Delaware Business Courts: Litigation Leadership" (2009) 34:3 *Journal of Corporation Law*.779.
[61]Bruner (2010) Virginia *Journal of International Law* 594.
[62]B Black & R Kraakman "Delaware 's Takeover Law: The Uncertain Search for Hidden Value'' (2002) *North Western University School of Law Vol. 9*6, No. 2. 558.
[63]559.
[64]DA Oesterle *The Law of Mergers and Acquisitions* (2005) 31.

Gorris, Hamermesh and Strine,[65] state:

> "[T]here has been a constructive symbiosis between the Model Business Corporation Act ("MBCA") and Delaware's corporation law, including its statutory component (the Delaware General Corporation Law, or DGCL) and its case law."

In most instances, the courts in the State of Delaware regulate takeovers.[66] The Delaware courts act quickly and efficiently. It has been indicated that

> "[T] ime is of the essence with all corporate matters considered by our Court of Chancery. Businesses need quick answers so they can move to the next step in their transactions."[67]

The Delaware Court of Chancery is the oldest business court in the US. The five members of the Court of Chancery sit without a jury and provide a decision at the conclusion of each judicial proceeding. Appeals from this court go directly to the Delaware Supreme Court and not to the Delaware Superior Court.[68] The decisions of the Chancery Court are well reasoned and the majority of the decisions are respected, and not generally appealed.[69] The BJR is regarded as one of the best examples of the Delaware judiciary's well-established corporate jurisprudence.[70] According to the internal affairs doctrine relating to states, the decisions of the Delaware courts are final and authoritative in matters of corporate law, if the corporation is registered in the State of Delaware.[71]

[65]JM Gorris, LA Hamermesh & LE Strine "Delaware Corporate Law and Model Business Corporations Act: A Study in Symbiosis" (2011) 74 *Law and Contemporary Problems* 107. <http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=1612&context=lcp> (Accessed 20-12-2014).
[66]JA Armour & DA Skeel, Jr. "Who writes the rules for hostile takeovers, and why? - the peculiar divergence of US and UK Takeover Regulation (2007) 95 The Georgetown Law Journal 1727, ECGI-Law Working Paper No.73/29006. 1729, Available at SSRN: https://ssrn.com/abstract=928928. (Accessed 5-2-2017).
[67]See Interview with Editor in *Metropolitan Corporate Counsel 2004* "The Hon. Myron T Steele: Delaware Courts, Corporate Governance and Corporate Counsel" Metropolitan Corporate Counsel (Delaware) 43.
[68]See Holland (2009) *The Journal of Corporation Law* 773.
[69]773.
[70]773.
[71]781.

However, the role of the courts in adjudicating disputes in mergers and takeovers has been criticized as it only allows for *ex post facto* dispute resolution.[72]

2 3 2 The Williams Act of 1968, the Securities Exchange Act of 1934 and the Securities Exchange Commission

The Williams Act of 1968 (Williams Act)[73] a federal government statute, provides for procedural and disclosure framework during tender offers in the US. The Williams Act effected a number of amendments and introduced other provisions into the Securities Exchange Act of 1934 in order to address cash tender offers and mandates disclosure of information when such offers are made for stock purchases.[74] It is named after Senator Harrison Williams, who championed it. For the purposes of the dissertation, the discussions are limited to an overview of the Securities Exchange Act 1934 and the Williams Act. The Securities Exchange Act of 1934 created the US Securities Exchange Commission (SEC) in 1934.[75] According to Tyson, the Williams Act aimed at introducing a policy of neutrality: it is meant to be neutral between bidders and targets.[76] The Williams Act contains several provisions which attempt to create a level playing field between bidders, targets and shareholders by requiring disclosures on share dealings at an early stage[77] The Williams Act established the basic ground rules for tender offers.[78] Shareholders are empowered with

[72]Armour & Skeel, Jr (2007) *The George Town Law Journal*. 1729.
[73]Pub. L. No. 90-439, 82 Stat. 454 (1968). *Enacted by the Senate and House of Representatives of the United States of America.*
[74]The Williams Act introduced sections 13(d)–(e) and 14(d)-(f) into the Securities Exchange Act 34. See also GA Ferrarini & GP Miller "A Simple Theory of Takeover Regulation in the United States and Europe" (2009) 42 *Cornell International Law Journal* 304.
[75]Section 4 of the Securities Exchange Act of 1934.
[76]W C Tyson "The Proper Relationship Between Federal and State Law in the Regulation of Tender offers" (2014) Notre Dame Law Review 252, discussing the historical regulation of tender offers prior to the enactment Williams Act. See also Ferrarini & Miller (2009) *Cornell International Law Journal*. 304
[77]Section 14(d) and Schedule14d-1 requires filings of disclosures with the Securities Exchange Commission as soon as 5 percent or more shares are acquired. See also Ferrarini & Miller (2009) *Cornell International Law Journal* 304.
[78]See Section 14(d)-(e) of the Securities Exchange Act and Schedule 14d-1, which specify the disclosures required.

full and complete information to make a decision about a tender offer[79] The Williams Act created an obligation to register any cash tender offer with the SEC; created obligations for disclosure of the value of the offer, the source of the funding, why the offer is being made, what plans the purchasers have for the newly-acquired company and any contracts or understandings that have been formed in regard to the target corporation.[80] The Williams Act also introduced a similar disclosures and filing for tender offers for more than 5 percent of a class of registered equity security, as those requested by the SEC under Schedule 14d-1.[81] The information is then made available to shareholders and other investors[82] By means of the disclosures, the Williams Act promotes transparency when share purchases are undertaken.[83] The Williams Act also prohibits any use of false, incomplete or misleading statements when making a cash tender offer.[84] This is in the interests of the investing parties. According to Ferrarini and Miller, under the Williams Act there is no direct right to sue for non-compliance but the courts have recognised the right for bidders, targets and shareholders. Such parties may apply to court to enforce the Act and the relevant regulations. .[85]

It is suggested that the Williams Act was enacted in response to the concern about the possibility that an acquiring shareholder may expropriate the wealth of the company.[86] These concerns also led to similar legislation in other countries. In enacting the Williams Act, the legislature wanted to avoid the pressure tactics being applied by bidders by launching unfair and coercive

[79]See Schedule 14d-1 and also Ferrarini & Miller (2009) *Cornell International Law Journal* 304-305.
[80]See Schedule14d-1 under the Securities Exchange Act and also Ferrarini & Miller (2009) *Cornell International Law Journal*. 304.
[81]Schedule 13d and also Ferrarini & Miller (2009) *Cornell International Law Journal* 305..
[82]See rules 14d-1 to Schedule 14D-9F under the Securities Exchange Act and also Ferrarini & Miller (2009) *Cornell International Law Journal* 305.
[83]Rules 14d-1 to Schedule14D-9F under the Securities Exchange Act. .
[84]Rule 10b-5 under the Securities Exchange Act and section 14(e) of the Securities Exchange Act are antifraud provisions. See also Ferrarini & Miller (2009) *Cornell International Law Journal* 305.
[85]Ferrarini & Miller (2009) *Cornell International Law Journal* 304.
[86]RB Thompson "Takeover Regulation After the 'Convergence' of Corporate Law" *(2002) Vanderbilt University Law School Law & Economics Working Paper* Number 02- 26 6.

takeover offers.[87] Prior to these reforms, bidders used 'short-lived public offers', known as 'Saturday night specials'[88] or 'Blitzkrieg tender offers'.[89] By means of sudden, undisclosed offers, bidders would buy limited amounts of a target stock on a first-come, first-served basis and at a substantial premium. Such 'Saturday night specials' did not indicate the intention of the acquirer or the future plans of the acquirer with the acquired company. They were often launched suddenly and with an element of surprise, which pressured shareholders to accept the offer.[90]

Tender offers were often "strategically abusive",[91] leading to unfavourable treatment of target company shareholders. Bidders often offered shareholders a high price for their shares on a "first-come first-served" basis for a very limited time period.[92] This increased shareholder uncertainty and fear that if they did not act quickly, they would be left holding shares which are difficult to sell or may be subject to a 'squeeze out' merger at a lower price.[93] This is because following the tender offer and subject to meeting the requisite thresholds, a bidder may acquire the shares of the shareholders who did not accept the tender offer which is also known as 'minority buy-out', "going private transactions", "cash out" "squeeze-outs" or "freeze-outs."[94] The shareholder must control at least 90 percent of the target shares to implement the freeze out.[95] Squeeze-outs are aimed at eliminating minority shareholders following a

[87]Thompson (2002) *Vanderbilt University Law School Law & Economics Working Paper* Number 02-26 6.
[88]"Saturday night specials" have been defined as a tender offer that is open for only a short period of time, typically just a few days, thereby forcing shareholders to decide quickly whether or not to accept an offer. The fear of losing out and the uncertainty forced shareholders to accept unfair offers. See G Subramanian "Bargaining in the Shadow of Takeover Defences" (2003) *Harvard John M Olin Center for Law, Economics, and Business Discussion Paper* No 9/2003. 9 <http://www.law.harvard.edu/programs/olin_center> (Accessed 20-2-2016).
[89]S Hannes & O Yadlin "The SEC Regulation of Takeovers: Some Doubts from a Game Theory Perspective and a Proposal for Reform" (2008) 25 *Yale Journal on Regulation* 42.
[90]Oesterle *The Law of Mergers and Acquisitions* 162.
[91]JA Armour, JB Jacobs & CJ Milhaupt "The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework" (2011) 52 *Harvard International Law Journal* Number 1 Winter. 241.
[92]Armour *et al* (2011) *Harvard International Law Journal* 241.
[93]See Armour *et al* (2011) *Harvard International Law Journal* 241.
[94]See F Restrepo & G Subramanian "The Effect of Delaware Doctrine on Freezeout Structures & Outcomes: Evidence on the Unified Approach" (2015) 5 *Harvard Business Law Review* 208.
[95]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law Vol.30 438.*

tender offer or a statutory merger.[96] The transactions are typically implemented as a merger, but can be a tender offer directly to shareholders.

Freeze-outs have an element of self-dealing because the controlling shareholder is the buyer and may have majority representatives on the target board.[97] Hence, the transactions have become subject to the entire fairness judicial review standard in Delaware courts.[98] The entire fairness standard is discussed below in paragraph 2 5 1 below. The aim of the “first come first served” tactics was to put pressure on and stampede target company shareholders into accepting the offer, even if the offer was low.[99] The short time period allowed to accept the offer also prevented target company directors from being able to take any evasive or defensive action against an unfair offer.[100]

A number of provisions in the Williams Act have been criticised. It is indicated that these provisions prevent some tender offers that would lead to the replacement of inefficient and poor performing managers.[101] If there are no threats of tender offers, it is likely that managers may avoid their duties and responsibilities knowing that there is no tool to discipline them.[102] Requiring various disclosures, the Williams Act may discourage tender offers due to the fact that bidders may feel that they will have to show their strategic plans to the target, and possibly to other competitors.[103] Further, bidders may be unwilling to make the first move to propose a takeover due to costs involved. The so-called ‘free rider’ effect results from this situation where competing bidders jump on the bandwagon, figuratively speaking, and simply interfere with the first bidder’s tender offer once they have seen the disclosures.[104]

[96]Restrepo & Subramanian 2015 *Harvard Business Law Review* 208.
[97]209.
[98]209.
[99]Armour *et al* (2011) *Harvard International Law Journal* 241.
[100]241-242.
[101]See Oesterle *The Law of Mergers and Acquisitions* 169.
[102]169.
[103]169.
[104]169.

Further criticism against the Williams Act is that the time periods introduced allows managers to undertake defensive measures or even place a competing bid.[105] A number of rules introduced by the SEC under the Williams Act are also criticised. These include the rule that there should not be any price discrimination in takeovers. It is argued that this rule increases the price of acquiring control.[106] Efficient takeover bids could be facilitated at low cost by repealing some of the provisions of the Williams Act. This in turn, would encourage managers to perform, as they fear the possibility of "Saturday night specials".[107] The SEC administers other statutes intended to protect investors and consumers.[108] The SEC has wide powers to regulate disclosure about tender offers and proxies, as part of protecting investors and ensuring that firms provides reliable information and set clear rules and regulations.[109] The role of the SEC among others, is to protect investors, maintain fair, orderly, and efficient markets, and also facilitate raising of capital in US financial markets.[110]

With broad powers over a number of industries, the duties of the SEC are extensive and among others, include to: interpret and enforce federal securities laws; issue new rules and amend existing rules; oversee the inspection of securities firms, brokers, investment advisers, and ratings agencies; oversee

[105] 169.
[106] 169.
[107] 169.
[108] See section 2 of Securities Exchange Act providing the reasons for the passing the Securities Exchange Act. The section describes a number of areas in which the Act apply. Section 3(a) (47) of the Securities Exchange Act also indicates a number of laws administered by the SEC. These includes: the Securities Act of 1933, the Securities Exchange Act of 1934, the Sarbanes-Oxley Act of 200219, the Trust Indenture Act of 1939, the Investment Company Act of 1940, the Investment Advisers Act of 1940, and the Securities Investor Protection Act of 1970.
[109] The SEC under section 4 of the Securities Exchange Act may prescribe rules and regulations, including those dealing with regulation of tender offers and proxies.
These appear under, Title 17, Securities and Commodities, Chapter II, Securities Exchange Commission, Part 240. General rules and regulations, under Securities Exchange Act 34, Published on the Electronic Code of Federal Regulations: Available at: https://www.ecfr.gov/cgi/bin/textidx?SID=0aa0a0af5bbc34f913fff4940d387537&mc=true&tpl=/ecfrbrowse/Title17/17cfr240_main_02.tpl, Accessed 2 .2. 2019.
[110] See the preamble to Securities Exchange Act., Section 3 (f) of the Securities Exchange Act which provides: "CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking, or in the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation."

private regulatory organisations in the securities, accounting, and auditing fields; and coordinate US securities regulation with federal, state, and foreign authorities. It was created to regulate a wide spectrum of the securities industry.[111] The SEC has wide powers to enforce the Williams Act. These include: issuing cease and desist orders,[112] administration actions,[113] civil actions for disgorgement,[114] or criminal actions through the Department of Justice.[115]

The Division of Corporation Finance reviews documents that publicly-held companies are required to file with the SEC. The documents include: registration statements for newly-offered securities; annual and quarterly filings; proxy documents sent to shareholders before an annual meeting; documents concerning tender offers; and filings related to mergers and acquisitions.[116] It is suggested that, through the Corporate Finance Division's review process and monitoring of compliance with disclosure requirements, the SEC seeks to improve the quality of the disclosure. The SEC also requires a number of disclosures about tender offers and proxies. These include: the offer price, a statement on whether the offer price is below the market price, any changes to offer price, the ability of bidder to finance the offer, identity of the bidder, plans or proposals of the offeror, and conditions and terms on the offer.[117]

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[111] See section 2 of Securities Exchange Act providing the reasons for the passing the Securities Exchange Act. The section describes a number of areas in which the Act apply. Section 3(a)(47) of the Securities Exchange Act also indicates a number of laws administered by the SEC. These includes: the Securities Act of 1933, the Securities Exchange Act of 1934, the Sarbanes-Oxley Act of 200219, the Trust Indenture Act of 1939, the Investment Company Act of 1940, the Investment Advisers Act of 1940, and the Securities Investor Protection Act of 1970.

[112] Section 21C of the Securities Exchange Act, also RJ Colombo "Effectuating Disclosure Under the Williams Act" (2011) 60 *Catholic University Law Review* 321-328.

[113] Section 15 (c) (4) and 21 C of the Securities Exchange Act

[114] Section 21C of the Securities Exchange Act, See also Colombo (2011) *Catholic University Law Review* 321-328.

[115] Section 21(d)(1) of the Securities Exchange Act. See also Colombo (2011) 60 *Catholic University Law Review* 321-328.

[116] See Regulation14A that deals with solicitation of proxies and the information to be included.

[117] Regulation 14D and Regulation 14E dealing with tender offers and the information to be included including the scope of both regulations, and also Oesterle, *The Law of Mergers and Acquisitions* 166.

2 4 An overview: Types of takeovers and mergers

2 4 1 An overview of the statutory merger, a ''long form merger,''[118] or a "one step freeze-out''[119] merger

The fundamental aim of US securities laws is to protect US investors. Therefore, transactions conducted there or employing US jurisdictional means may be subject to US securities laws.[120] The structuring of a transaction is therefore important.[121] Practitioners generally rely on Delaware case law to structure takeovers and mergers.[122] Some of the important considerations are: whether any of the parties are subject to US securities laws or whether the securities holders of any of the parties are located or residents in the US.[123] Tender offers and sale of corporate control are regarded as key mechanisms for replacing inefficient and nonperforming managers. Corporate assets can be allocated for higher and better use following a successful takeover.[124] The takeover or merger processes will also depend on the size and number of shareholders, among other considerations. The bidder will generally undertake research and due diligence on the target company before deciding on the best method to undertake a takeover or merger.[125]

There are number of transactions that allow controlling shareholders to appropriate equity interests of minority shareholders using a freeze-out namely: statutory mergers, two-step tender offers, and asset acquisitions or reverse stock splits.[126] However, reverse stock split and asset sales are rarely used to

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[118] See Wachtell, Lipton, Rosen & Katz (2018) Takeover Law and Practice.74. Available at: http://www.wlrk.com/ (Accessed 10-5-2018).
[119] See Ventoruzzo (2010) *Virginia Journal of International Law* 852.
[120] JM Basnage & WJ Curtin, III "Cross-border tender offers and other business combination transactions and the U.S federal securities laws: an overview" (2016) 71:2 *The Business Lawyer* 462.
[121] 520.
[122] See MJ McGuiness & T Rehbock "Going Private Transactions: A Practitioner's Guide" (2005) 30 *Delaware Journal of Corporate Law* 437.
[123] 462.
[124] Sepe (2010) *Arizona Legal Studies Discussion Paper 10-29* 14.
[125] 6-7.
[126] See Restrepo & Subramanian (2015) *Harvard Business Law Review* 208 and also M Ventoruzzo "Freeze-Outs: Transcontinental Analysis and Reform Proposals" (2010) *50:4 Virginia Journal of International Law* 851.

cash out minority shareholders.[127] According to McGuiness & Rehbock,[128] there are two distinct methods of implementing a takeover or a merger and then delisting a company from an exchange that merit close consideration by practitioners in this area of law.[129] The methods can be classified as the "traditional approach", which is carried out following negotiations between the acquirer and the target company, followed by a merger agreement[130] and, the "unilateral approach", which is carried out by the acquirer who sets the price terms and conditions of the tender offer and, makes the offer directly to the shareholders. [131]

The board of directors are gatekeepers in respect of statutory mergers. Board approval creates an insurmountable barrier for a statutory merger if the board is unwilling to co-operate.[132] Therefore, there would be no merger without the board say so.[133] It is not possible to propose a hostile statutory merger.[134] Developments over the years have caused the terms and conditions used in one-step transactions and those used in two- step transactions to converge: they are essentially becoming one exercise.[135] Both tender offers and statutory mergers may raise fiduciary duties of directors. Directors must always observe their fiduciary duties during the negotiations.[136] This point will be discussed below under paragraph 2 5, dealing with the standards used by the courts to review the conduct of directors during takeovers and mergers.

A statutory merger is a long-form single-step transaction and a creature of statute.[137] In essence, the statutory merger is the purchase of all the assets and

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[127]Ventoruzzo (2010) *Virginia Journal of International Law* 851.
[128]McGuiness & Rehbock (2005) Delaware Journal 437.
[129]437.
[130]438.
[131]437-438
[132]S Bainbridge "The Geography of Revlonland" (2013) 81 *Fordham Law Review* 3280.
[133]3286.
[134]3286.
[135]See RE Climan, GR Bason, Jr, FS Green and JI Greenberg "Negotiating Acquisitions of Public Companies in Transactions Structured As Friendly Tender Offers" *(2012) 116:3 Penn State Law Review* 671.
[136]See Bainbridge (2013) *Fordham Law Journal* 3277-3338.
[137]Wachtell, Lipton, Rosen & Katz (2018) Takeover Law and Practice74.

an assumption of all liabilities of one entity by another.[138] The separate legal existence of one of the merging entities ceases on implementation of the merger by operation of law.[139] The Delaware statutory merger provisions are generally referred to as the business combination acts by the business community.[140] The DGCL in section 251 provides for the long-form merger procedure. The provision sets the framework and requirements to complete all mergers and consolidations.[141] One of the effects of mergers is its impact on the legal status, rights, liabilities and powers of the merged or consolidated entities. A merger may negatively affect existing rights and status of parties after the merger, unless properly regulated.

The DGCL has a number of sections dealing with legal status, rights, liabilities, powers and other similar rights or obligations of the merged, surviving or liquidated entities following a merger or consolidation.[142] The DGCL provisions are also tailored to the different characteristics of corporations that may merge or consolidate their operations. The DGCL includes provisions aimed at foreign companies that merge or consolidate with US companies.[143] In addition, the SEC has adopted regulation aimed at addressing conflicts between US and foreign regulations.[144] The regulations introduced relief for certain cross-border tender offers and business combinations. Prior to the regulations it was common for bidders to exclude US investors in cross–border tender offers and business combinations. [145] The regulations introduce certain limited exemptions under Tier I and Tier II exemptions. Each Tier indicates the level and type of exemption limitations granted.[146]

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[138]74.
[139]74.
[140]DA Oesterle "Delaware's Takeover Statute: Of Chills, Pills, Standstills, and Who Gets Iced" (1988) 13 *Delaware Journal of Corporate Law* 879.
[141]See section 251 of DGCL.
[142]See sections 259, 260 and 261 of the DGCL.
[143]See sections 256 and 258 of the DGCL dealing with mergers or consolidations of domestic and foreign companies.
[144]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 469.
[145]469
[146]469-470.

Briefly, the ‘long-form’ procedure entails a number of steps. The acquirer announces the intention to acquire the shares held by minority shareholders of the listed company.[147] The target company must then form an independent special committee to negotiate the terms and conditions of the merger. The special committee is an integral part of the traditional approach method.[148] The special committee must have independent and disinterested directors.[149] It appears that the target company may have to appoint additional directors where it does not have a sufficient number of independent directors.[150] Legal and financial advisers, who must only report to it, so as to maintain independence, may assist the special committee.[151]

The special committee is obliged to negotiate on an arm-length basis with the acquirer to fulfil its mandate and must not let the controlling shareholders dictate the terms and conditions of the merger agreement. The responsibility of the special committee is to promote the interests of minority shareholders.[152] Once negotiations have been successful, the special committee will recommend a merger agreement setting out the terms and conditions of the merger, to the board. The board of the acquirer and the target company will sign the merger agreement setting out all the terms and conditions including the obligations of each party and the timelines. The target company and the acquirer will then complete the merger based on the agreement.[153] The target company must then prepare an information or proxy statement and seek shareholder approval for the merger.[154] A statutory merger requires approval of shareholders of the target company and must therefore comply with the proxy rules issued by the SEC.[155] The target company is obliged to prepare and file a proxy statement

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[147]437.
[148]445.
[149]The courts may review the process followed by directors during a takeover. See also discussions dealing with standards of reviewing directors’ conduct under paragraph 2 5 below.
[150]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 445.
[151]445.
[152]445.
[153]445.
[154]445.
[155]Proxy Rules are made in terms of section 14(a) of the Securities Exchange Act and the rules promulgated by the SEC in terms of the Securities Exchange Act. See Regulation 14A, solicitation of proxies and also Wachtell, Lipton Rosen & Katz (2018) *Takeover Law and Practice* 64.

with the SEC.[156] The proxy statement provides information to the target shareholders about the proposed meeting of shareholders to consider and approve the statutory merger. The SEC may review the proxy statement prior to it being posted to the target shareholders.[157] Some of the important disclosures in the proxy statement include: background to the transaction; a summary of material terms of the merger; historical transactions and interactions between the parties; brief reasons why the board of directors of the target company has agreed to and is recommending the proposed merger; background to the transaction; financial information from the acquirer where financing is not guaranteed; and a brief indication of any reports, opinions or appraisals provided to the directors of the target in respect of the proposed merger.[158]

As part of the disclosures, the SEC requires explanation of the procedures followed when investment bankers prepare a fairness opinion, including banker's opinions and any limitations to such opinions.[159] Statutory mergers are also subject to additional disclosure information about appraisal rights.[160] Statutory mergers have certain advantages and disadvantages.

Advantages for the bidder include:

- support by the independent and disinterested special committee board members. This may encourage unwilling shareholders to submit their form of acceptance for the offer;[161]

[156]Regulation14A deals with solicitation of proxies and the information to be included. See also SM Davidoff Solomon "The SEC and the Failure of Federal Takeover Regulation" (2007) 34:2 *Florida University State Law Review* 235. 227 and Wachtell, Lipton Rosen & Katz (2018) *Takeover Law and Practice* 75.

[157]Wachtell, Lipton Rosen & Katz (2018) *Takeover Law and Practice* 74.

[158]See section 14(a) of the Securities Exchange Act and the rules promulgated by the SEC in terms of the Securities Exchange Act and also Wachtell, Lipton Rosen & Katz (2018) *Takeover Law and Practice* 64.

[159]Wachtell, Lipton Rosen & Katz (2018) *Takeover Law and Practice* 64.

[160]Section 262 of DGCL on appraisal rights.

[161]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law Vol.30* 458.

- where a well- functioning special committee on advice of legal advisers and financial advisers has properly conducted the process, it has a strong likelihood of withstanding a court challenge;[162]
- the approach allows the controlling shareholders to complete the transaction even if it does not acquire more than 90 percent of the issued shares of the target because some shareholders do not tender their shares.[163]

The disadvantages for the bidder include:
- it increases the risk of the transaction taking longer or failing, due to prolonged negotiations;[164]
- it may increase costs as the acquirer may be forced to increase the offer price so that the special committee, and then the board recommend the merger[165];
- the transaction is subject to a higher standard of review- the entire fairness standard, and therefore may attract more shareholder litigation than a transaction subject to a lower standard of review.[166]

The decision as to which method to use depends on the circumstances of each transaction.[167] It appears that practitioners prefer to use a statutory merger where it is expected that there will be delay and complications due to the number of regulatory requirements involved.[168] The issue of own securities as a method of payment for a merger or takeover may result in such a delay. This is because the issue of own shares may require registration of a statement or prospectus in terms of the Securities Act of 1933, unless exempted.[169] Payment of cash does not require any additional registration and therefore there are no delays to the merger. It is also indicated that under certain circumstances the statutory merger may have a tax advantage, particularly where the acquirer is

[162]458.
[163]458.
[164]459.
[165]459.
[166]449.
[167]Wachtell, Lipton, Rosen & Katz (2018) *Takeover Law and Practice* 75.
[168]75.
[169]See Basnage & Curtin III (2016) *The Business Lawyer* 468.

paying by issuing its own shares as shareholders benefit from a rollover tax relief.[170]

2 4 2 An overview of tender offers and the "two step freeze outs"[171]

Where a company has widely dispersed shareholders, control of a company may be achieved by making a tender offer to the shareholders.[172] The SEC has "erected a scaffold" [173] of rules which are generally applicable to tender offers, going private transactions and takeover transactions. The SEC's approach to regulation of tender offers is to allow shareholders to make an informed decision about their investment, based on disclosures about the tender offer.

The concept 'tender offer' is not defined in the Williams Act.[174] The SEC has been reluctant to provide a guideline as to what 'tenders offers' are. The reluctance by the SEC to provide such guidance is due to the concern that precise definition would encourage bidders to attempt to avoid the provisions.[175] Rule 14d-2 is the only SEC rule that gives an indication of what tender offers entail. However, the rule merely defines when a tender offer commences.[176] A purchaser may acquire shares of a company without triggering the tender offer rules.[177] Certain factors may support a conclusion that one is undertaking a tender offer. These include: widespread invitation to buy shares of a company; acquisitions of shares of a company at a premium over the market price; offers to acquire shares of a company open for a limited period; offer to acquire a substantial shareholding; firm offers to acquire shares

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[170]Basnage & Curtin III (2016) *The Business Lawyer* 516 and also Wachtell, Lipton, Rosen & Katz (2018) *Takeover Law and Practice* 93.
[171]Ventoruzzo (2010) *Virginia Journal of International Law* 852. The tender offer involves an initial acquisition of 90 percent of target shares and then followed by acquisition of the remaining shares hence the term two step freeze-out. See also Climan *et al* (*2012) Penn State Law Review* 618.
[172]See Sepe (2010) *Arizona Legal Studies Discussion Paper 10-29* 6-7.
[173]Davidoff Solomon (2007) *Florida University State Law Review* 235.
[174]Oesterle *The Law of Mergers and Acquisitions* 173.
[175]173.
[176]173.
[177]Basnage & Curtin, III (2016) *The Business Lawyer* 466.

which are not negotiable; or public announcements to acquire shares accompanied by rapid accumulation of shares.[178]

Under the Unilateral Approach tender offer, the bidder determines the price, terms and conditions of the tender offer without initial discussions with the board of the target. The tender offer is then made directly to shareholders.[179] The tender offer may be subject to a condition that the bidder holds 90 percent of the target shares at the end of the transaction. This will enable the bidder to effect a short- form merger or the 'freeze-out' merger after the tender offer.[180] In friendly tender offers, the bidder and the target company may include a provision in the agreement that following the completion of the tender offer, a merger will be concluded without shareholder approval in accordance with section 251(h) of the DGCL.[181] Where parties will implement the merger in terms of section 251(h) of the DGCL, the tender offer is commonly conditional on acceptance by the majority of the shareholders.[182] If the tender offer meets this condition, then the transaction may be implemented in accordance with the requirements of section 251(h) of the DGCL.[183] Section 251(h) facilitates completion of a second-step merger by removing the requirement for a shareholder approval to complete the second-step merger.[184] Prior to this section, shareholder vote was required to effect a second-step merger even if the acquirer had received acceptances of the tender offer exceeding the majority of the issued shares.[185]

The implementation of the merger in terms section 251(h) is subject to a number of conditions. These include: that all shares to be acquired must be acquired for the same amount and kind of consideration as in the tender offer and; the offer is extended to all outstanding shares of the target.[186] The section

[178]466-467.
[179]See McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 437-438.
[180]See Wachtell, Lipton, Rosen & Katz (2018) *Takeover Law Practice* 74.
[181]74.
[182]74.
[183]74
[184]76.
[185]77.
[186]77.

allows the bidder and the target company to consummate the transaction quickly and with certainty.[187] In a Unilateral Approach tender offer, if the bidder holds more than 90 percent of the issued shares of the target when the tender offer ends, it can then proceed to the second step 'short form merger'.[188] Where the bidder and the target have agreed to implement the transaction in terms of section 251(h), then if the transaction meets those conditions, the bidder will be entitled to implement a 'second step merger'. This explains the reference to 'two-step mergers' or 'two-step freeze-outs'.[189]

The takeover process may also be accompanied by market purchases prior to the tender offer being made and in terms of the Williams Act these should comply with certain disclosure requirements.[190] The Williams Act provides a framework for disclosures in respect of the acquisitions referred to above, while the rules of the SEC set-out certain rules about those acquisitions.[191] The disclosures in terms of the SEC regulations and rules depend on the type of transactions.[192] The requirements include that: the tender offer statement, the response statement from the target, the tender offer must remain open for acceptance for at least 20 business days from the date of opening;[193] where the tender offer price is changed, the tender offer must be kept open for a minimum of 10 additional business days after the price has changed;[194] and, shareholders must have a right to withdraw from the tender offer.[195]

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[187]77.
[188]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 438.
[189]See CW Furlow "Reflections on the Revlon Doctrine" *(2009) 11:3 U. of Pennsylvania Journal of Business Law* at 546 discussing Unocal Corp. v. Mesa Co 493 A.2d 946 (Del.1985) case and the two-step merger procedure.
[190]Section 14(d), Regulation 14D of the Securities Exchange Act applies to certain tender offers and Schedule 13D under the Securities Exchange Act is also applicable on acquisition of 5 percent or more of securities of a company. See also Ferrarini & Miller (2009) *Cornell International Law Journal* 304-305.
[191]Section 14(e) of the Securities Exchange Act and Regulation 14E. The regulation also includes a number of rules dealing with tender offers. See rules 14e-1 to 14f-1, indicating certain unlawful tender practices.
[192]For instance, transactions that requires shareholder meetings must comply with Regulation 14A dealing with solicitations of proxies, while Schedule TO under section 14(d)(1) of the Securities Exchange Act applies to tender offers.
[193]Rule 14d-1(a) of the Securities Exchange Act and Basnage & Curtin III (2016) *The Business Lawyer* 480.
[194]480-481.
[195]Solomon (2007) *Florida University State Law Review* 218.

A party seeking to make a tender offer is obliged to prepare and file with the SEC a disclosure statement in terms of SEC rules for tender offers, where the offer is for registered securities.[196] The majority of target companies appoint a special committee to consider the tender offers even though it is not mandated by law.[197] Tender offers are mainly governed by section 14(d) and section 14(e) of the Securities Exchange Act. Section 14(d) and the SEC rules provide for detailed disclosure obligations, procedural requirements and other substantive provisions for tender offer.[198] Exemptions and exclusions may be available for tender offers.[199] In general, the tender offer rules do not require the SEC to pre-review tender document to shareholders. However, where there is a conflict with non-US rules, it may be necessary to apply to the SEC in advance.[200] The disclosures required by SEC in the relevant forms are incorporated by the acquirer in the offer document, which is then sent to the shareholders of the target company.[201] Financial information about the target company is not required where the offer consists of only cash.[202] Disclosures assist shareholders in making better-informed decisions, and deter abuse.[203]

The SEC imposes additional disclosure requirements on acquirers who intend to take a company private.[204] It has been observed that the promulgation of the rule was in reaction to what the SEC regarded as inadequate protection offered by Delaware State laws.[205] The additional disclosures include: a statement of

[196] Schedule TO, under the Securities Exchange Actand the target issues a response on Schedule 14D-9. See discussion by Basnage & Curtin III (2016) *The Business Lawyer* 467.
[197]See McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 445.
[198]See among others, Section 14(d) and Regulation 14D, applicable to tender offers involving a class of equity securities (as defined in the Securities Exchange Act) and section 14(e) of the Exchange Act and regulation 14E, which are aimed at preventing fraud and manipulation. See also Basnage & Curtin III (2016) *The Business Lawyer* 467.
[199]Section 3(a) (10) of the Securities Exchange Act and Basnage & Curtin III (2016) *The Business Lawyer* 467.
[200]See Clifford Chance LLP “General overview of US Tender Offer rules Applicable to an Offer for Shares Registered under the Securities Act of 1934” (2014) *Global M&A series.*
[201]See Schedule TO under the Securities Exchange Act.
[202]Clifford Chance (2014) *Global M&A Series*.1.
[203]HTC Hu “Too complex to Depict? Innovation, Pure Information and the SEC Disclosure Paradigm” (2012) 90:7 *Texas Law Review.* 1615.
[204]Rule 13e-3 of the Securities Exchange Act.
[205]See M Roe “Delaware’s Competition” (2003) 117 *Harv. L. Rev*. 588.

whether the transaction is fair to the independent shareholders, a detailed description of the transaction, the reasons for the transaction, an opinion from an independent financial adviser dealing with the fairness of the transaction and, a brief report on all the opinions received by the target company, including any financial reports from its own financial advisers.[206]

The SEC rules restricts purchases of the target company's shares, other than pursuant to the tender offer, from the first public announcement by the acquirer of its intention to make the tender offer until the tender offer has been completed.[207] A bidder must not acquire shares on the open market while the bid is still open.[208] A bidder may obtain irrevocable commitments from shareholders to accept a tender offer.[209] The SEC also enforces the 'all price rule', which requires that the price offered for the tendered shares must be the same for all shareholders.[210] The purpose of the rule is to prevent coercive and unfair treatment tender offers similar to an 'early bird special', where shareholders who tendered their shares early received a higher offer.[211] All tender offers are subject to the general anti-fraud provisions. Untrue statements, omission of material information or misleading statements are prohibited. In addition, deceptive, manipulative practices and pressure tactics due to short time periods are not allowed.[212] Other restrictions on tender offers relate to antitrust legislation when the acquisition of shares of a particular value is made or assets.[213] The discussions of the impact of takeover and mergers on different industries, and how they may be affected by antitrust authorities' rules are beyond the scope of the dissertation.

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[206]Rule 13e-3 of the Securities Exchange Act and also See Basnage & Curtin III (2016) *The Business Lawyer* 489-490.
[207]Rule 14e -5 of the Securities Exchange Act, Act, and Basnage & Curtin III (2016) *The Business Lawyer* 484.
[208]Rule 14e-5 of the Securities Exchange Act and also Basnage & Curtin III (2016) *The Business Lawyer* 484.
[209]See Rule 14d-10 of the Securities Exchange Act and also Basnage & Curtin III (2016) *The Business Lawyer* 487-488.
[210]Rule d-10(a) (1) of the Securities Exchange Act requires the tender offer to be open to all the shareholders of the target, irrespective of their location. See also Basnage & Curtin III (2016) *The Business Lawyer* 497.
[211]Climan *et al (2012) Penn State Law Review* 628.
[212]Basnage & Curtin III 2016 *The Business Lawyer* 484.
[213]See Ferrarini & Miller (2009) *Cornell International Law Journal* 305.

A freeze-out following a tender offer that has been structured properly under the Unilateral Approach will be subject to a judicial review standard under the deferential BJR.[214] This is in contrast to a freeze-out following a traditional approach transaction, which is subject to the heightened entire fairness standard of review.[215] Other scholars indicate that conflicted controlling stockholder transactions are generally subject to the entire fairness standard of review. Exceptions may include: making conflicted controlling stockholder transactions subject to the approval of, an effective special committee, or minority shareholders which may shift the burden of proving entire fairness standards to the plaintiff. Furthermore, subjecting such transactions from the beginning to the approval of both an effective special committee and minority shareholders in a fully informed, uncoerced vote may lower the standard of review to business judgment.[216] The standards of reviewing actions of directors are discussed below in paragraph 2 5.

In deciding which method to adopt in effecting a takeover or merger, practitioners consider the method with least disadvantages.[217] The Unilateral Approach method has both advantages and disadvantages. Advantages for the bidder include:

- it is not subject to the heighted entire fairness standard of judicial review[218];
- it avoids time consuming and intricate negotiations with the target special committee. The bidder may continue even after the committee rejects the offer.[219] Speed and timing appears to be the major advantage of the tender offer (it can be consummated quickly);[220] and;

[214]See McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law Vol.30* 438.
[215]438.
[216]Wachtell, Lipton, Rosen & Katz (2018) *Takeover Law and Practice* 43.
[217]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 458.
[218]459.
[219]459.
[220]See Climan *et al (2012) Penn State Law Review* 621-622 and, at 626.

- further, the bidder is able to change and modify the terms of the offer unilaterally.[221]

The Unilateral Approach also has disadvantages, which include:

- that an offer in terms of this approach may be negatively perceived by the market that the offer from the bidder does not have support of the target company directors;[222]
- that it may be difficult for a bidder to raise funding to acquire all outstanding shares of the target;[223]
- if the bidder does not succeed in achieving the 90 percent threshold to implement a squeeze out after the offer, it may be forced to take another step such as the statutory merger, to complete the takeover. This may result in additional costs for the bidder as it is forced to make another offer to enable it to implement the squeeze out.[224]

2 4 3 An overview of hostile and unsolicited tender offers

As discussed in the previous paragraph 2 4 2, a bidder may make a tender offer directly to the shareholders without negotiating with directors of the target company. The directors of the target company, whose shareholders have received an offer directly from the bidder without their co-operation, may take a number of steps to prevent the offer from succeeding. This can lead to hostilities between the bidder and directors of the target company. A hostile takeover primarily refers to a change in corporate control against the wishes of the incumbent management and the board of directors. Morck, Shleifer and Vishny[225] refer to a hostile takeover as an acquisition where:

[221] McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 459.
[222] 459.
[223] 459.
[224] 460.
[225] RK Morck, A Shleifer & RW Vishny "Characteristics of Targets of Hostile and Friendly Takeovers" in AJ Auerbach, (ed) *Corporate Takeovers: Causes and Consequences* (1988) 101–136. <http://www.nber.org/books/auer88-1. (Accessed 2-8-2014.)

> "[T]he initial bid for the target was neither negotiated with its board prior to being made nor accepted by the board as made. Thus, initial rejection by the target's board is taken as evidence of the bidder's hostility, as is active management resistance to the bid, escape to a "white knight,"[226] or a management buyout in response to unsolicited pressure"[227]

Thompson[228] quotes Shleifer & Vishny who say, "Takeovers are widely interpreted as the critical corporate governance mechanism in the US, without which managerial discretion cannot be controlled." Takeovers are regarded as a method of monitoring and disciplining management. It is difficult to acquire control of companies whose majority shares are held by a single shareholder or groupings without the co-operation of that shareholder. This may lead to a hostile takeover.[229] A proxy contest may also be used to achieve a takeover.[230] Prior to the 1960s, the primary method to force a change of corporate control in the US was to launch a proxy contest and then remove the incumbent board.[231] As the name suggests, proxy contests are a form of hostile takeover although a tender to acquire the shares may or may not be involved. Shareholders are entitled to nominate directors whom they believe may better serve the company and all its shareholders.[232] The attempt to replace the incumbent directors may result in an election contest between the newly-nominated directors and existing directors.[233] Unsuccessful hostile tender offers led to bidders formulating new strategies to overcome the defensive poison pills.[234] A new phenomenon has developed over a number of years where both a hostile tender offer and proxy contests are used jointly as part of

[226]A "white knight" refers to a friendly acquirer who has been invited by target management to increase the offer price or make an offer on better terms than those offered by an unwelcome bidder. See A Shleifer & RW Vishny "Greenmail, white knights, and shareholder's interests" (1986) 17: 3 *Rand Journal of Economics* 294.

[227]Morck *et al* in *Corporate Takeovers: Causes and Consequences* 101 -136.

[228]Thompson (2002) *Vanderbilt University Law School Law & Economics Working Paper Number* 02-26. 3.

[229]Schuster (2010) *LSE Law* 2.

[230]239*.*

[231]239.

[232]M Lipton & SA Rosenblaum "Election Contests in the Company's Proxy: An Idea Whose Time has Not Come" (2003) *The Business Lawyer.*69.

[233]69.

[234]Armour *et al* (2011) *Harvard International Law Journal* 247.

a well-coordinated takeover strategy.[235] This is one of the effective strategies because the bidder will be able to remove the existing target directors and replace them with its nominated directors. The bidder's nominees would then be able to remove the poison pill defence and ensure the success of the hostile takeover.[236]

The federal law applicable here is section 14(a) of the Securities Exchange Act of 1934, together with the SEC's proxy rules. Proxy contests must comply with SEC rules.[237] It is asserted that the SEC's proxy rules are the most important regulations in proxy contests and the courts are also significant as this is where parties can seek relief against any inequitable conduct on the part of the board. The SEC's proxy rules require a proxy statement with all solicitations for voting.[238] The rules also provide how proxies should be obtained. Hostile tender offers have gradually replaced proxy contests as a means to achieve corporate control.[239] One of the reasons for this is that the tender offer may be implemented quickly and also allows the bidder to recover a portion of his costs should the bid not be successful. The shares acquired can possibly be sold at a profit in the stock market.[240]

2 5 An overview: The standards of reviewing the decisions of board of directors during takeovers and mergers.

The State of Delaware has a more developed and sophisticated body of precedent-setting cases on corporate law issues than other states in the US.[241] There are a number of reasons for this, including the expertise of the judges in a limited jurisdiction trial court, the presence of the Delaware Chancery Court (a court with limited jurisdiction that is able to hear only matters of corporate

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[235]239.
[236]247.
[237]Regulation14A of the Securities Exchange Act, deals with proxies and see also the discussions under paragraph 2 4 2.
[238]Regulation 14A of the Securities Exchange Act and Schedule 14A. See also Oesterle *The Law of Mergers and Acquisitions* 158.
[239]Armour *et al* (2011) *Harvard International Law Journal* 240.
[240]240.
[241]Oesterle *The Law of Mergers and Acquisitions* 31.

law), and the fact that most publicly-held companies have their place of registration as Delaware, even if they have only limited business dealings within the state. Cases on mergers and acquisitions have contributed significantly to the protection of shareholders, as they are able to rely on those cases in pursuit of their rights to the courts.[242] As the DGCL is an enabling statute, the enforcement of the director's fiduciary duties is one of the most important checks the Delaware judiciary imposes to guard against managerial abuse.[243] When shareholders believe that directors have breached their fiduciary duties, they can file a suit with the Delaware Court of Chancery.[244] The courts have also developed standards of reviewing directors' decision-making process in a number of transactions. It has been indicated that the terminology is not accurate and is:

> "[S]omewhat misleading, because in corporate law the standard of review is not the familiar civil procedure standard that governs how a higher court or other tribunal should review the decision of a lower tribunal. Rather, in corporation law, the term refers to the substantive standard that courts apply in deciding whether challenged board action constitutes an actionable breach of fiduciary duty."[245]

There are three standards of reviewing actions of directors namely: the entire fairness standard discussed under paragraph 2 5 1 below, the intermediate standards of review discussed in paragraph 2 5 2 below and the BJR discussed below under paragraph 2 5 3.[246] Initially, there were only two standards of review- the entire fairness standard and the BJR. These two standards are regarded as the bedrock of standards of review in corporation law in Delaware.[247]

[242]Oesterle *The Law of Mergers and Acquisitions* 31.
[243]LE Strine "The Delaware Way: How We Do Corporate Law and Some of The New Challenges We (And Europe) Face" (2005) 30 *Delaware Journal of Corporate Law* 681
[244]681.
[245]JB Jacobs "Fifty Years of Corporate Law Evolution: A Delaware Judge's Retrospective" (2015)5 *Harvard Business Law Review* 154.
[246]154-155.
[247]155.

2 5 1 The entire fairness standard of review

The entire fairness standard of review is the strictest level of judicial review of the decisions of the board.[248] One of the landmark cases[249] in respect of the entire fairness standard is the case of *Weinberger v UOP.*[250] This case is regarded as a seminal case in respect of the entire fairness standards where freeze-out mergers are involved.[251] The *Weinberger* case clarified the type of protection that minority shareholders should enjoy in freeze-out mergers. The case involved a freeze-out merger transaction with a majority shareholder. Briefly, the facts are that, Weinberger, a former shareholder of UOP Inc., brought a suit against the directors of UOP Inc. challenging a merger between the company and its majority shareholder - The Signal Companies Inc.

As a result of the merger, minority shareholders were bought out for cash. In its final ruling, the Chancery Court held that the terms of the merger were fair to Weinberger and other minority shareholders, and ruled in favour of the defendants. On appeal, the Delaware Supreme Court held that, while it agreed with part of the Chancery Court ruling that the majority shareholder must prove that the transaction was fair, the plaintiff must first demonstrate some action as a basis for invoking the fairness obligation.[252] The court also determined that since no measures were taken to provide for arm's length negotiations, the appropriate standard of review was the entire fairness standard. The court further pointed out that in a parent-subsidiary context, where it is shown that the negotiations were done on an arms-length basis, each party exerting and having bargaining power against the other, this would serve as strong evidence that the transaction meets the test of fairness. The court further added that

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[248]SV Scott & S Brody "The Evolving Role of Special Committees in M&A Transactions: Seeking Business Judgment Rule Protection in the Context of Controlling Shareholder Transactions and Other Corporate Transactions Involving Conflicts of interest" (2014) 69 *The Business Lawyer* 1121.
[249]McGuiness & Rehbock (2005) *Delaware Journal of Corporate Law* 441.
[250]Weinberger v. UOP Inc., 457 A.2d 701 (Del. 1983).
[251]Subramanian "Fixing Freeze-outs" (2004) *Harvard Law School John M Olin Center for Law, Economics and Business Discussion Pap*er Series. Paper 501, 4.
http://isr.nellco.org/harvard_olin/501> (Accessed 20-2-2016).
[252]Weinberger v. UOP Inc., 457 A.2d 701 703 (Del. 1983).

where a transaction has been voted on by an informed vote of a majority of the minority shareholders then, the burden of proving that the transaction is unfair to minorities entirely shifts to the plaintiff.[253] Parties who rely on the fact that minority shareholders have voted in favour of a transaction must show that they have completely disclosed all material facts relevant to the transaction.[254] The entire fairness standard requires both “fair dealing” and a “fair price”. The court pointed out that:

> “The concept of fairness has two basic aspects: fair dealing and fair price. The former embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained. The latter aspect of fairness relates to the economic and financial considerations of the proposed merger, including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock.”[255]

The court then pointed out that in this matter, the record does not support a finding that the minority shareholders’ vote was an informed one. This is due to the fact that material information necessary for the minority shareholders to bargain with UOP Inc. and the majority shareholders was withheld. This amounted to breach of the directors’ fiduciary duties. Therefore, the court concluded that the merger did not meet the test of fairness.[256] The matter was then referred to the Delaware Chancery to decide on the fair value of the shares.

[253]Weinberger v. UOP Inc., 457 A.2d 701 703 (Del. 1983).
[254]703.
[255]711.
[256]703.

2 5 2 The intermediate standard of review

The Williams Act does not regulate the conduct of the directors of the target company as the ‘‘board neutrality rule’’[257] does in the UK’s takeover regime.[258] The regulation of the conduct of directors during takeovers and mergers is therefore undertaken through various state laws.[259] In particular, the State of Delaware came to be seen as the chief architect of such rules. The courts regulated such conduct on a case-by-case basis.[260] The intermediate standards rules did not develop systematically until after 1985.[261] In the period between 1985 and 1988, the Delaware courts developed three intermediate standards of reviewing directors’ decisions based, on common law judicial decision-making.[262] These standards add a higher level of judicial scrutiny, also referred to as “enhanced business judgment”[263] standard of judicial review. The intermediate standards of judicial review dealt with instances where the board, subject to a hostile takeover bid, adopted defensive actions and opposed the takeover bid. The question as to who should decide a hostile offer between the board and the shareholders is not clear-cut.[264] Some of the questions to be answered are:

> “[W] ho should decide whether an unsolicited takeover bid can go forward – the stockholders or the target company board, and which governmental branch – the executive, legislative, or judicial – should decide the first question?” [265]

[257]The Board Neutrality rule provides that when a tender offer is launched, the directors of the target cannot initiate or continue any action that might frustrate the success of an offer without the approval of shareholders in a meeting. M Ventoruzzo “Takeover Regulation as a Wolf in Sheep’s Clothing: Taking U.K Rules to Continental Europe” (2008) 11:1 *U. Pennsylvania Journal of Business Law* 135 141.
[258]Armour *et al* (2011) *Harvard International Law Journal* 259.
[259]259.
[260]262.
[261]243.
[262]245.
[263]See S Bainbridge “Unocal At 20: Director Primacy in Corporate Takeovers” 2005 31 *Delaware Journal of Corporation Law* 31.
[264]Armour e*t al* (2011) *Harvard International Law Journal* 243.
[265]243.

The State of Delaware has not made any pronouncements on either issue, but historically the courts have always ruled on the conduct of directors during takeovers, and this is settled at least in the State of Delaware.[266] Where the takeover bid takes the form of a proposal for a merger, the DGCL provides that the board had powers to decide whether or not shareholders may vote on the merger. This is in line with the basic principles set out in DGCL in section 141(a), relating to directors' powers to manage the affairs and business of corporations.[267] Where a transaction involves a tender offer, the DGCL does not vest any statutory power in the board.[268]

The issue of defensive tactics during a takeover was a focal point in the matter of *Unocal Corp. v Mesa Petroleum Co.*[269] The Delaware Supreme Court decided the case on the basis of fiduciary duties of directors. The court held that the directors have fiduciary duties to interpose themselves between the bidder and the shareholders and, if necessary, to take defensive action which is not disproportionate to the threat posed by the takeover. The decision in the *Unocal* case[270] created a new standard to measure directors' duties during a hostile takeover. One of the concerns the court had was that hostile offers create potential for conflict of interest. As the court puts it, because of the "omnipresent specter that a board may be acting primarily in its own interests rather than those of the corporation and its shareholders",[271] it is imperative that such a tender offer be subject to additional judicial scrutiny. Briefly, the facts in the *Unocal* case are as follows: The appellant, defendant in the court of first instance, Unocal Corp. (Unocal), appealed the decision of the Court of Chancery where the court had ruled in favour of the plaintiff, Mesa Petroleum Co (Mesa). Mesa held approximately 13 percent of the issued shares of Unocal. Mesa attempted to launch a buy-out of Unocal in a two-stepped transaction. The board of Unocal rejected the offer on the basis that it was unfair and not

[266] 242.
[267] Section 141(a) of the DGCL provides that "the business and affairs of every corporation … shall be managed by or under the direction of a board of directors". This prevents possible meddling and interference on directors' actions by shareholders in the day-to-day operation of the corporations without due course.
[268] Armour *et al* (2011) *Harvard International Law Journal* 243.
[269] 493 A.2d 946 (Del. 1985).
[270] 493 A.2d 946 (Del. 1985).
[271] 493 A.2d 946 (Del. 1985).

for the benefit of shareholders. It did so after taking a number of steps to consider the offer, including taking advice from financial advisers. The advice received was that the offer was grossly inadequate. Based on this advice, the board adopted a defensive strategy against the hostile bid. As part of a defensive tactic against the hostile offer, the board introduced a self-tender of its own shares (share repurchase). The share repurchase would exclude the shares held by Mesa. In addition, the share repurchase would require Unocal to incur debt, as it would raise money to be used for the share repurchase. The directors considered the matter and concluded that the action is reasonable and the company can afford the debt. Mesa then launched an application seeking an injunction against the actions of the board in respect of the share repurchase. Mesa claimed that the share repurchase that excluded it was not legally permissible. The Court of Chancery agreed. On appeal, the Delaware Supreme Court disagreed and ruled that a blanket prohibition of this kind of practice could not be maintained. The court ruled that:

> "The factual findings of the Vice Chancellor, fully supported by the record, establish that Unocal's board, consisting of a majority of independent directors, acted in good faith, and after reasonable investigation found that Mesa's tender offer was both inadequate and coercive. Under the circumstances the board had both the power and duty to oppose a bid perceived to be harmful to the corporate enterprise. On this record we are satisfied that the device Unocal adopted is reasonable in relation to the threat posed, and that the board acted in the proper exercise of sound business judgment."[272]

In summing up the reasons for its decision and reversing the decision of the Chancery Court, the Supreme Court highlighted a number of important factors. The Supreme Court indicated that it would not substitute the decision of the board for its own, if that decision can be "attributed to any rational business purpose." [273] This was because the board of Unocal had a broad authority upon which to make decisions. Its duties and responsibilities are based on the inherent powers conferred by section 141(a) of the DGCL. In terms of this

[272] 493 A.2d 946, (Del. 1985).
[273] 493 A.2d 946, (Del. 1985).

section, the affairs and business of a corporation are under the management of the board. A Delaware corporation may validly deal selectively with its shareholders, on condition that the directors have not acted out of sole or primary purpose to entrench themselves in office to the exclusion of shareholders.[274] The board has a fundamental duty to protect the corporation from harm, irrespective of where it may come from. The board has an obligation to respond to the offer in a manner that is in the best interests of the company and its shareholders.[275] In its ruling, the Delaware Supreme Court referred to the BJR,[276] and indicated that unless shown on preponderance of evidence that the directors' decisions were aimed at perpetuating themselves in office, or some other breach of fiduciary duty such as fraud, overreaching, lack of good faith or being uninformed, the court cannot substitute its decision. Here the court applied the BJR and the directors had the benefit of the BJR based on the presumption that when they made their decisions they acted: (1) on an informed basis, (2) in good faith, and (3) in the honest belief that the action taken was in the best interest of the company.[277] Directors were able to avoid the enhanced scrutiny by complying with these requirements.[278] With this ruling, the court created the enhanced BJR to guard against the potential conflicts faced by the directors. However, the standard has been diluted over time.[279]

In another matter dealing with defensive tactics during a takeover is *Revlon Inc. v MacAndrews & Forbes Holdings, Inc*.[280] The court had to decide whether the standard of reviewing directors' conduct in defending a hostile takeover created in the *Unocal case*, namely, "the enhanced scrutiny", was applicable.[281] Briefly, the facts in Revlon are: Revlon's board was faced with the threat of a hostile

[274]493 A.2d 946, (Del. 1985)
[275]493 A2d 946, (Del. 1985)
[276]493 A.2d 946, (Del. 1985)
[277]493 A.2d 946, (Del. 1985)
[278]I Anabtawi "The Twilight of Enhanced Scrutiny in Delaware M&A Jurisprudence" (January 2019, Forthcom*ing)* 43, Delaware Journal of Corporate Law 10; *UCLA School of Law, Law & Economics Research Paper Series Research Paper No 18-11* Available at SSRN: https://ssrn.com/abstract=3248474.Accessed (20 -11-2018.)
[279]Anabtawi (January 2019 Forthcoming) Delaware Journal of Corporate Law 10.
[280]*Revlon Inc. v MacAndrews & Forbes Holdings, Inc* 506 A.2d 173 (Del.1986).
[281]Bainbridge (2013) *Fordham L. Rev* 3297.

takeover by Pantry Pride, a subsidiary of MacAndrews & Forbes Holdings Inc. (the bidder). The board implemented several defensive measures, including a poison pill[282] and, a share repurchases in exchange for promissory notes and preference shares (the initial defensive measures). In addition, the board searched for another bidder as a "white knight"[283] (the second defensive measures). Forstmann Little & Co became the white knight and agreed to acquire Revlon. The agreement had numerous provisions to protect the transaction from another bidder. The terms of the merger agreement included a no-shop clause,[284] a termination fee,[285] and a lock-up option. [286] The lock-up option gave Forstmann Little & Co the right to buy two divisions of Revlon for significantly less than market value should another bidder buy 40 percent or more of Revlon's shares. The bidder then approached the Chancery Court for an injunction against the transaction which was granted. On appeal the Delaware Supreme Court agreed with the board of *Revlon* and upheld the initial defensive measures taken by the board. The Supreme Court indicated that directors defending a takeover may be protected by the BJR, provided they can

[282]A poison pill refers to various defensive measures adopted by boards of directors in response to a takeover attempt or in advance of a possible takeover attempt which may cause severe economic repercussions in the acquirer or the potential controlling person. See SS Dawson, RJ Pence & DJ Stone "Poison Pill Defensive Measures" (1987) 42: 2 *The Business Lawyer* 423-439 423. There is no doubt that the sale of the two divisions at 40 percent discount will devalue the target company and thereby cause potential financial harm to the competing bidder.

[283]See definition of "white knight" at note 262 above. A Shleifer & RW Vishny "Greenmail, white knights, and shareholder's interests" (1986) 17: 3 *Rand Journal of Economics* 294.

[284]"No-shop clause" also called "no talk" is an agreement to negotiate only with one party. A typical exclusivity provision requires the grantor not to `initiate contact with, solicit, encourage or participate in any way in discussions or negotiations with, or provide information to a competing bidder. Under this type of clause, the directors of the target are forbidden from taking any action, such as seeking or considering an alternative offer, even higher bid, which would render the consummation of the transaction under lock up less likely. See J Mayanja "No-shop, No Talk and Break-up Fees Agreements in merger and takeover Transactions: The case for a fresh regulatory approach" (2002) *Australian Journal of Corporate Law* 6-7.

[285]A termination fee refers to a fee that is usually payable by the target company whose directors have agreed to support a negotiated acquisition transaction by the bidder to a bidder if the transaction is not implemented in accordance with the agreed terms as a result of certain clearly defined events. See JQ Jeon & JA Ligon "How much is reasonable? The size of termination fees in mergers and acquisitions" (2011)17*Journal of Corporate Finance* 959-981.959, termination fees are also called break fees or reimbursement fees.

[286]"Lock up device" refers to an option granted at the discretion of target management, which gives a selected bidder the right to purchase a portion of a target at a discount. It allows target managers to simultaneously advocate an acquisition by one party and obstruct attempts by others. See TR Burch "Locking out rival bidders: The use of lockup options in corporate mergers" (2001) 60 *Journal of Financial Economics* 103-141 104.

establish that they meet the requirements for relying on it.[287] The court also indicated that:

> "Where directors have decided to commit the corporation to a change of control transaction, their actions must be evaluated solely by reference to their duty to obtain the highest value reasonably available."[288]

The reason for the court to uphold the initial defensive tactics adopted by the board of Revlon was that the directors acted to protect the shareholders against a low, unfair price while retaining the flexibility to accept any higher offer that may be received. Therefore, the defensive action taken was regarded as reasonable considering the threat posed by the hostile bid.[289] Rejecting the second line of defensive tactics adopted by the board, the court indicated:

> "[T]he Revlon board's authorization permitting management to negotiate a merger or buyout with a third party was a recognition that the company was for sale. The duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit. This significantly altered the board's responsibilities under the *Unocal* standards. It no longer faced threats to corporate policy and effectiveness, or to the stockholders' interests, from a grossly inadequate bid. The whole question of defensive measures became moot. The directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.'' [290]

The court then considered the lock-up option defensive tactic. The defensive measure gave Forstmann Little & Co the right to buy two divisions of Revlon for significantly less than market value should another bidder buy 40 percent or more of Revlon's shares. The court found that the board were no longer acting in the interest of shareholders to maximise shareholder value when it concluded

[287]506 A.2d 173 181 (Del.1986).
[288]WT Allen, JB Jacobs & LE Strine Jr "Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law" (2001) 26 *Delaware Journal of Corporate Law* 893.
[289]506 A.2d 173 181 (Del.1986).
[290]506 A.2d 173 182 (Del.1986).

this scheme. The board should have been aware that the company was for sale and their duties were to obtain a higher price for shareholders.[291] The board breached their duty of care to shareholders and their actions were potentially detrimental to the interest of shareholders.[292] The lock-up device as a defensive tactic had the effect of ending the auctioning of the shares of Revlon to the detriment of shareholders, even though the bidder had increased the offer price.[293] The bidder could no longer proceed with the takeover offer, thereby denying shareholders an opportunity to get a higher price.[294] The defensive tactics adopted by the board of Revlon was tainted by directors' interests and directors had breached their fiduciary duties.[295] The court concluded that this defensive measure is contrary to a duty of care and the directors were not entitled to protection under the BJR.[296] This defensive measure was invalidated.[297] The court also ruled against the 'no-shop clause' in the agreement as it prevented the board from negotiating with other bidders. The court concluded that target shareholders are entitled to the best price available. Therefore, market forces should be allowed to operate freely in order for directors to obtain best prices for shareholders. [298] The decision of the court created what is generally referred to as the 'Revlon doctrine', under the Delaware law.[299] The Revlon doctrine is applicable when the board of directors considers the sale of a company or a change of control.[300] The Revlon doctrine has two important implications. These are:

> "First, the focus of the board's fiduciary duties shifts from the long-term well-being of the corporation to the short-term interests of the stockholders in achieving a transaction that will maximize the value of their shares. These refocused duties are frequently referred to as Revlon duties. Second, the Court

[291] 506 A.2d 173 182 (Del.1986).
[292] 506 A.2d 173 182 (Del.1986).
[293] 506 A.2d 173 183 (Del.1986).
[294] 506 A.2d 173 179 (Del.1986)
[295] 506 A.2d 173 185 (Del.1986).
[296] 506 A.2d 173 184 (Del.1986).
[297] See S Bainbridge "The Geography of Revlon-Land" (2013) 81 *Fordham Law Review* 3298-3299.
[298] 506 A.2d 173 184 (Del.1986).
[299] CW Burlow "Reflections on the Revlon Doctrine" (2009) 11:3 *U. of Pennsylvania Journal of Business Law* 520.
[300] 523.

> will subject the board's performance of its Revlon duties to enhanced scrutiny, even though, under the business judgment rule, the decision would be entitled to judicial deference." [301]

The following situation will trigger Revlon principles:

> "(1) the target's board initiates an active bidding process to sell the corporation or to effect a business reorganization involving a clear breakup of the company;
> (2) in response to an initial offer, the target's board causes the corporation to abandon the corporation's long-term strategy and seeks an alternative transaction involving the breakup of the company;
> (3) the transaction results in a sale or change of control of the corporation."[302]

The *Revlon* case created a standard of review of the conduct of directors during takeovers or mergers in terms of which the judicial deference created by the BJR, generally given to board decisions narrows from rationality to a range of reasonableness.[303] Under the Revlon doctrine, in the sale for cash payment, the court closely scrutinises the price paid and the process followed by the board.[304] This is done to ensure that no other considerations were taken into account by the board, other than ensuring that the shareholders obtain the highest price.[305] Bainbridge noted that, the *Revlon* standard created a number of problems and the courts initially "waffled"[306] on the matter as to what exactly are the Revlon standards of review. The precise geography of *Revlon* standards of judicial review is still unclear.[307]

The obligation imposed on directors, to obtain the best price for shareholders, as imposed in the *Revlon case* was further clarified in another case, *In re Smurfit-Stone Container Corp. Shareholder Litigation,*[308] where shareholders

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[301]523.
[302]Bainbridge (2013) *Fordham Law Review* 3337-3338.
[303]JT Laster "Revlon is a Standard of Review: Why it's True and What it Means" 19 (2013-2014) *Fordham J. Copr & Fin. L* 6.
[304]Harvard Law Review "Recent Cases" (2012) 125 *Harvard Law Review* 1256.
[305]Harvard Law Review "Recent Cases" (2012) 125 *Harvard Law Review* 1256.
[306]Bainbridge (2013) *Fordham Law Review* 3299.
[307]3317.
[308]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011).

would receive shares in another company as part of the consideration for selling their shares. In this matter, the court applied the principles set out in the *Revlon case* where a consideration for acquiring shares in a negotiated merger was split equally between a cash and share payment.[309] Briefly, the Court of Chancery had to consider an application for an injunction against a merger transaction entered into by the board of Smurfit–Stone Container Corp, where the merging company had no controlling shareholder, by a shareholder who alleged breach of fiduciary duties by directors.[310] Plaintiff contended that the transaction is subject to the Revlon principles as the directors had put the company of up for sale.[311]

In essence, the argument was that the directors are obliged to obtain the highest price for the shareholders in line with the *Revlon case.* In this case, shareholders were to receive a combination of cash and shares, in equal proportions as a consideration.[312] The court had to consider whether the standard for reviewing directors' duties is the enhanced scrutiny set in terms of the *Revlon case* or the deference rule in terms of the BJR.[313] The Delaware Chancery court considered the applicable principles established in the *Revlon case* and held that even though payment was split equally in cash and shares of the acquirer, and the company had no controlling shareholder, the Revlon doctrine applied.[314] The court indicated that "the concern here is that there is no "tomorrow" for approximately 50% of each stockholder's investment in Smurfit-Stone".[315] According to the court, for a Smurfit shareholder, that is the end of the game for a substantial investment in a Delaware corporation.[316] The transaction will result in the end of the corporation.[317] The decision is criticised as having a potential to discourage the target board from agreeing to

[309]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011), See also Harvard Law Review "Recent Cases" (2012) 125 *Harvard Law Review* 1256.
[310]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011) 23-25.
[311]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011) 26.
[312]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011).26-27.
[313]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011) 28, and in Harvard Law Review "Recent Cases" (2012) 125 *Harvard Law Review* 1256.
[314]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011) 40.
[315]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011) 36.
[316]No. 6164-VCP, 2011 WL 2028076 (Del. Ch. May 24, 2011 36.
[317]Harvard Law Review "Recent Cases" (2012) 125 *Harvard Law Review* 1257.

transactions that could be beneficial to shareholders where payment is split equally in cash and shares.[318]

It is pointed out that the original *Revlon case* dealt with cash payment, the court can easily establish whether shareholders were paid the highest price.[319] In transactions involving shares and share mergers, the BJR applies because the board is in a better position to decide on the merits of such transactions.[320] A court cannot declare that one proposal is better than the other based only on shares as the future value depends on the financial health of the acquirer and profits of the combined company.[321] Similarly, in a mixed consideration transaction with equal shares and cash, the value of the merger is not easily determinable.[322]

Applying the Revlon doctrine in the scenario requires the court to evaluate the strategies of the parties, to determine the value of the transaction post the merger. Target boards are in a better position to evaluate this fact rather than the courts.[323] While the court found that the directors in the matter had properly carried out their duties, the decision is criticised, and it is submitted by scholars that the court should not have applied the enhanced scrutiny principle as set out in the *Revlon case*. It is argued that taking into consideration the process followed by the directors in this case, directors had exercised their duties faithfully.[324] It is asserted that:

> "Corporate law would have been better served if the Court of Chancery had refrained from applying *Revlon* case to the Smurfit-Stone transaction and instead deferred to the business judgment of the disinterested directors, who could best determine whether the Rock-Tenn transaction was in the interest of Smurfit-Stone shareholders."[325]

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[318] 1261.
[319] 1264.
[320] 1264.
[321] 1264.
[322] 1264.
[323] 1264.
[324] 1258.
[325] 1265.

Another important matter relating to the application of the BJR in mergers, decided by the Chancery Court, is *In re MFW Shareholder Litigation.*[326] The Chancery Court had to deal with a case where the majority shareholder wanted to buy out the remaining shares. The offer by the controlling shareholder was subject to two main conditions, namely: approval by an independent special committee of the board of directors, and approval by the majority of the minority shareholders.[327]

Certain shareholders sued the directors and the controlling shareholders on the basis that the transaction was unfair, and attempted to interdict voting at the shareholders meeting. However, the litigants abandoned the initial claims and eventually sued for damages on the basis of breach of fiduciary duties by directors. The plaintiff argued that the transaction should be subject to the "entire fairness procedure,"[328] rather than the deferential BJR. The defendants argued that the transaction should only be subject the BJR due to the specific procedures set by the controlling shareholder prior to the merger discussions. The Court of Chancery agreed with the defendants and dismissed the claim. The rationale of the court was that the two procedures, which were pre-conditions for the merger, were correctly followed. The court further ruled that the BJR should,

> "[O]nly be invoked if:
> (i) the controller conditions the transaction on the approval of both a Special Committee and a majority of the minority stockholders;
> (ii) the Special Committee is independent;
> (iii) the Special Committee is empowered to freely select its own advisors and to say no definitively;
> (iv) the Special Committee acts with care;
> (v) the minority vote is informed; and
> (vi) there is no coercion of the minority."[329]

[326] 67 A.3d 496 (Del. Ch.2013).
[327] 507.
[328] See the discussions of the entire fairness standard in paragraphs 2 5 1.
[329] 67 A.3d 496 645 (Del. Ch.2013).

The court analysed the process followed in the transaction and indicated that the independent committee consisted of directors who were in law independent, and that the majority of the minority shareholders who voted in favour of the transaction were unconnected to the bidder.[330] The court held that it is appropriate to defer to the disinterested directors and shareholders whose money was at stake.[331] The courts are not business experts.[332] The members of the independent committee had an incentive to ensure that proper procedures were followed because they wished to protect their reputations. Therefore, they will be willing to negotiate for a buy-out price that is in the best interests of shareholders to ensure that shareholders will approve it.[333] The controlling shareholder also knowing that the independent committee who has no interest negotiates the transaction will likely accept their views since he is concerned that they are unlikely to recommend a transaction they consider not fair.[334] If the transaction is not recommended by the independent committee it may be rejected shareholders.[335] The majority of the minority shareholders on the other hand, have the opportunity to reject the deal based on the full disclosure and without any coercion.[336] For these reasons the court ruled in favour of the defendant. In an appeal against the ruling of the court of first instance, the Delaware Supreme Court in *Kahn v M & F Worldwide Corp (MFW)*,[337] endorsed the decision of the Court of Chancery in *in re MFW Shareholder Litigation*. The court confirmed that the standard of review that governs mergers between controlling shareholders and its subsidiary where the transaction *ab initio* was subject to both the approval of an independent sufficiently-empowered special committee of the board that fulfils its duty of care; and voted on by the majority of the minority who voted freely based on informed basis, is the BJR.[338] The court pointed out that the defendant must

[330] 500-503.
[331] 500-503.
[332] 525-527.
[333] 525-528.
[334] 528-530.
[335] 530-530.
[336] 528-530
[337] 88 A3d 635 (Del 2014).
[338] 88 A3d 635 (Del 2014).

prove that the transaction was fair to minority shareholders. The defendant may shift the burden of proof to the plaintiff by proving that: the transaction was approved by either a well-functioning independent board of directors, or the transaction was approved by an informed vote of a majority of the minority shareholders.[339] The full bench of the Delaware Supreme Court unanimously ruled that the more deferential business judgment rule standard of review, rather than the entire fairness standard of review applies to buy-outs by controlling shareholders, if the conditions for invoking the BJR stated by the Chancery Court in *In re MFW Shareholder Litigation,* as quoted above, were met. The court analysed the transaction process adopted by the board of MFW. It was noted that from the beginning of the transaction, MFW's board required that the proposal to effect a buy-out be undertaken on two conditions aimed at protecting shareholders. Firstly, the merger proposal was to be negotiated and approved by a special committee of independent MFW directors. Secondly, MFW required that the proposal be approved by a majority of shareholders not connected to MFW.[340] By subjecting the transaction to the above procedural steps ensured protection for minority investors against the potential conflict, because of the involvement of the controlling shareholder. Therefore, the court ruled that the directors did not breach their fiduciary duties, and were entitled to the protection of the more deferential BJR.[341]

Another matter that came before the Delaware Chancery court concerning defensive tactics in hostile takeovers is *Blasius Industries Inc. v Atlas Corporation.*[342] A matter dealing with proxy contests, in particular, the action of directors that are designed to interfere with the rights of shareholders to vote. The reaction of the target board in a proxy contest raises numerous issues, including fiduciary duties. As discussed above in paragraph 2 4 3 under hostile takeovers, proxy contests are a form of a hostile takeover. The main issue for the court to decide in the *Blasius case* was: which standard of reviewing the conduct of directors should be applied when a board take steps intended to

[339]88 A3d 635 642 (Del 2014).
[340]88 A3d 635 (Del 2014).
[341]88 A3d 635 (Del 2014).
[342]564 A.2d 651, 662-663 (Del. Ch. 1988).

interfere with the right of shareholders to vote, particularly the right to vote for a different board.[343] Briefly, the facts in the case are that Blasius Industries Inc (Blasius), a substantial shareholder, approached the board of Atlas Corporation (Atlas), with a number of proposals. Blasius requested the board to undertake various steps, including, shareholder voting on amendment of bylaws of Atlas, increasing the board and electing new board members representing Blasius, restructuring and repayment of capital.[344] The increase of the board would have resulted in directors representing Blasius being in the majority on the board of Atlas. This was viewed by the board of Atlas as an attempt to take control. The board of Atlas reacted by increasing the number of directors to ensure that Blasius does not have majority of directors on the board. The board of Atlas refused to co-operate with the other proposals and voted against them. *Blasius* sued on the basis that the directors did not act in good faith and their actions were motivated by selfish effort to protect their positions to collectively control Atlas. The defendants relied on the BJR, and asserted that they acted with due care and in good faith to protect the shareholders of Atlas from the threat of having an impractical, dangerous proposal being forced on them.[345] The court ruled that the BJR is not applicable where directors' actions interfere with shareholders votes, even if the decision of the directors was taken in good faith.[346] In the court's ruling, where a board took defensive actions which had the effect of interfering with shareholders' freedom to vote, the actions will be invalidated, unless the board can show a "compelling justification"[347] for taking such actions. The court held that there are policy justifications for adopting this rigorous standard. This is because directors are installed into office following a vote by shareholders. Directors' legitimacy to exercise their corporate powers is derived from being voted in by the shareholders. Therefore, it is important that the right of shareholders to vote should be protected against any interference by the board.[348] The *Blasius case* standards of reviewing the conduct of directors was designed to enforce that basic principle of company

[343] Armour *et al* (2011) *Harvard International Law Journal* 245.
[344] 564 A.2d 651, 654 (Del. Ch. 1988).
[345] 658-659.
[346] 651.
[347] 661.
[348] 564 A.2d 651, 657–663 (Del. Ch. 1988).

law.[349] According to Siegel,[350] the Delaware courts have applied the Blasius test to five other shareholder voting cases. The standard of judicial review of directors' conduct in respect of shareholder voting cases requires further "judicial pruning.''[351]

2 5 3 The business judgment rule

A decision by directors whether to enter into a transaction or not, is often complex and challenging. As indicated above in paragraph 2 5 above, Delaware judges introduced standards by which conduct of directors are evaluated when exercising their fiduciary duties. The BJR is one of these standards. The BJR protects directors who have reached their decisions, having acted fully informed, in good faith, without personal bias or interest, and with an honest belief that the action undertaken was in the best interest of the corporation and its stakeholders.[352] The BJR plays an important part in regulation of takeovers and mergers in the US, including in the State of Delaware. Therefore, it is appropriate that a section is dedicated to this rule. The BJR is not only applicable to takeovers and mergers but its reach is much broader, as it can be seen from case law discussed in this chapter.

The BJR has its origins in England and the 1742 matter of *Charitable Corp v Sutton 2 Atk,400,26 Eng.Rep*.642 (Ch.1742).[353] The Lord Chancellor of England indicated the court's unwillingness to second guess business decisions of directors. The BJR has been described as expressing a policy that directors' decisions may not be reviewed by judges if certain conditions exist.[354] In those cases, a judge determining adherence to BJR will consider if:

> "(i) a decision was made by directors (as opposed to incumbent management);

[349]Armour *et al* (2011) *Harvard International Law Journal* 247.
[350]M Siegel "The Problems and Promise of "Enhanced Business judgment" (2014) 17 *U. Pennsylvania Journal of Business Law* 189.
[351]184.
[352]WM Lafferty, MA Schmidt, & DA Wolfe Jr, "A brief Introduction to the Fiduciary Duties of Directors Under Delaware Law" (2012) 11 *Penn State Law Review* 839.
[353]Holland (2009) *University of Pennsylvania Journal of Business Law* 679.
[354]Allen Jacobs & Strine Jr (2001) *Delaware Journal of Corporate Law* 870.

(ii) the directors were disinterested and independent,

(iii) the directors acted in subjective good faith, and

(iv) applied a reasonable decision-making process."[355]

The BJR is a "logical common law corollary to the fundamental statutory principle, codified in section 141(a) of the DGCL that the business and affairs of a corporation are managed by its board of directors."[356] The BJR is designed to effect a compromise between two competing values: the need to hold board of directors accountable and their authority. Boards of directors should be held accountable but their discretionary powers must also be preserved.[357] The BJR is regarded as providing procedural guidance to litigants and also operate as a substantive rule of law. In making decisions, the board is presumed to have acted on an informed basis: in good faith and honestly in that the action taken is in the interests of the company. Where there is no breach of fiduciary duties, conflict of interest or bad faith, directors will be entitled to rely on the BJR.[358] Litigants who challenge the board's decision must rebut the presumption. Presenting facts showing that the directors have in fact acted disloyally, in bad faith, or with gross negligence can do this.[359] Wachtell, Lipton, Rosen & Katz[360] indicate that:

> "The purpose of the rule is to "encourage [ ] corporate fiduciaries to attempt to increase stockholder wealth by engaging in those risks that, in their business judgment, are in the best interest of the corporation 'without the debilitating fear that they will be held personally liable if the company experience losses''

The Delaware Supreme Court in *Aronson v Lewis,*[361] described the BJR as follows:

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[355]870.

[356]Holland (2008-2009) 34 *Journal of Corporation Law* 779.

[357]S Bainbridge "The Business Judgment Rule as Abstention Doctrine" (2004) 57.1 *Vanderbilt Law Review* 84.

[358]*Aronson v Lewis* 473 A.2d, 805, 812 (Del 1984).

[359]See Wachtell, Lipton, Rosen & Katz (2018) *Takeover Law and Practice* 29.

[360]See Wachtell, Lipton, Rosen & Katz (2018) T*akeover Law and Practice* 29. The footnote in the quote has been omitted.

[361]*Aronson v Lewis* 473 A.2d 805 (Del. 1984).

> "It is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. Absent an abuse of discretion, that judgment will be respected by the courts."[362]

Briefly, the facts in the *Aronson case* are as follows: the Delaware Supreme Court dealt with an appeal from the Chancery Court where a shareholder, acting on behalf of a company, challenged certain actions by the directors on the basis that they failed to comply with their fiduciary duties. Having succeeded at the court of first instance, the Delaware Supreme Court reversed the decision of the Chancery Court on appeal. In its ruling the Supreme Court emphasised the basic and important principle of the DGCL that directors of a corporation rather than shareholders, manage the business and affairs of the corporation as provided in terms of section 141(a) of the DGCL, except where the certificate of incorporation of the company provides otherwise. The court further added that these powers are also subject to certain fundamental fiduciary duties to the corporation. The court pointed out that the BJR is an acknowledgement of managerial prerogatives of Delaware directors under section 141(a). There is a presumption that in making a business decision, directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests the company. The courts will respect the decision and actions taken by directors where the directors did not abuse their discretion. Any party challenging the decision of the directors must rebut the presumption that the decision was properly made.[363]

Another important case on the BJR is that of *Smith v Van Gorkom (Van Gorkom case).*[364] The brief facts of the matter are that the directors of Transunion Corporation (the Company), a public company, agreed to sell the company to another company, New T Company, a wholly owned subsidiary of Mormon Group Inc, in a merger.[365] The agreement was that the shareholders of the Company would receive cash for their shares. The directors approved the

[362]473 A.2d 805,812 (Del. 1984).
[363]473 A 2d 805 (Del.1984).
[364]*Van Gorkom* Case 488 A.2d 858 (Del 1985).
[365]See *Van Gorkom* case 488 A.2d 858 (Del 1985) at 864.

merger and the shareholders of the Company approved the merger based on the disclosure provided by the directors. Some shareholders of the Company instituted a class action claiming damages from directors who had agreed to the merger of the Company.[366] The Chancery Court found that the board of directors had to be protected in terms of the BJR on the basis that when they made a decision to recommend a merger agreement to the shareholders, the directors were informed. However, the Delaware Supreme Court did not agree with this view and reversed the decision by majority rule decision.[367] The Supreme Court ruled (1) that the directors were not fully informed when they made the decision to recommend the merger agreement. (2) that the Board's subsequent efforts to amend the Merger Agreement and take other curative action were ineffectual, both legally and factually; and (3) that the Board did not deal with complete openness with the shareholders by not disclosing all material facts, which they knew or should have known, before securing the shareholders' approval of the merger. [368]

The court referred to the chronology of the events leading to the approval.[369] The Supreme Court found that the board of directors approved the merger proposal after a meeting lasting two hours and without seeing the written agreement. With the exception of two directors, the board was not informed about the purpose of the meeting until it was in session. The decision to merge was based primarily on a short oral presentation by Van Gorkom, the Chief Executive Officer and Chairman of Trans Union. The oral presentation was based on a merger agreement that Van Gorkom had not reviewed and he was not informed of the essential provisions. Van Gorkom generated the merger proposal in relative secrecy and never disclosed to the board how he came up with the merger price. The investment bankers for the company were not invited to the meeting. The board did not ask questions as to how the price was arrived at. The board was also not aware of the intrinsic value of the company as

[366]See *Van Gorkom* 488 A.2d 858 (Del 1985)
[367]*Van Gorkom* case 488 A.2d 858, (Del 1985) 863-864.
[368]*Van Gorkom* case 488 A.2d 858, (Del 1985) 863-864. See also BS Sharfman "The Enduring Legacy of Smith v van Gorkom" (2008) *Delaware Journal of Corporate Law* 291.
[369]See *Van Gorkom* case 488 A.2d 858, (Del 1985) 864-870.

compared to the merger price. None of the board members read the merger agreement before signing, and the final amendments did not correspond to the actual documents discussed with the board.[370] The Delaware Supreme Court did not agree with the decision taken by the board, more so because there was a likelihood that a higher offer price could have been secured for shareholders.[371] In order to support a contention that a business judgment decision by directors was an informed one, the directors should inform themselves before making a business decision, of all material information reasonably available to them. [372]

The court then indicated:

> "On the record before us, we must conclude that the Board of Directors did not reach an informed business judgment on September 20, 1980 in voting to 'sell' the Company for $55 per share pursuant to the Pritzker cash-out merger proposal. Our reasons, in summary, are as follows: 'The directors (1) did not adequately inform themselves as to Van Gorkom's role in forcing the "sale" of the Company and in establishing the per share purchase price; (2) were uninformed as to the intrinsic value of the Company; and (3) given these circumstances, at a minimum, were grossly negligent in approving the "sale" of the Company upon two hours' consideration, without prior notice, and without the exigency of a crisis or emergency."[373]

The court further indicated:

> "The defendants simply failed in their original duty of knowing, sharing, and disclosing information that was material and reasonably available for their discovery. They compounded that failure by their continued lack of candour in the Supplemental Proxy Statement."[374]

The court added:

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[370]*Van Gorkom* case 488 A.2d 858, (Del 1985) 864-870.
[371]See L Lederman 'Deconstructing *Lyondell*: Reconstructing *Revlon'* (2010/2011) *New York Law School Law Review* 645. Analysing the rationale of the court.
[372]*Van Gorkom* case 488 A.2d 858 (Del 1985) 872.
[373]*Van Gorkom* 488 A.2d 858 (del 1985) 874.
[374]*Van Gorkom* 488 A.2d 858 (Del 1985) 893.

> "For the foregoing reasons, we conclude that the director defendants breached their fiduciary duty of candour by their failure to make true and correct disclosures of all information they had, or should have had, material to the transaction submitted for stockholder approval."

In conclusion, the court stated:

> "To summarize: we hold that the directors of Trans Union breached their fiduciary duty to their *stockholders* (1) by their failure to inform themselves of all information reasonably available to them and relevant to their decision to recommend the Pritzker merger; and (2) by their failure to disclose all material information such as a reasonable *stockholder* would consider important in deciding whether to approve the Pritzker offer"[375]

Accordingly, the Delaware Supreme Court held that the Chancery Court, erred in applying the business judgment rule in favour of the directors of Trans Union in this case.[376] The court ordered that the Court of Chancery conduct an evidentiary hearing to determine the fair value of the shares represented by the plaintiffs' class, based on the intrinsic value of Trans Union on September 20, 1980. Following that, an award of damages may be entered to the extent that the fair value of Trans Union exceeds the price paid under the merger agreement.[377]

The case is possibly the most famous case decided by the Delaware Supreme Court.[378] The *Van Gorkom case* shows the important role the board must play during negotiations for a takeover or merger. The court in this case found directors grossly negligent in approving an arm's length sale of the company as they failed to inform themselves about the value of the transaction.[379] This was

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[375]See *Van Gorkom* 488 A.2d 858 (Del 1985) 893.
[376]*Van Gorkom* 488 A.2d 858 (Del 1985) 893.
[377]*Van Gorkom* 488 A.2d 858 (Del 1985) 893.
[378]Sharfman (2008) 33 *Delaware Journal of Corporate Law* 287.
[379]BS Sharfman "Fine Tuning Gross Negligence Twenty Plus Years After VanGorkom" (*November 2006) 62:1The Business Lawyer* 149-151.

despite the fact that shareholders overwhelmingly supported the merger after detailed disclosures were made.

In light of this court ruling, it could be concluded that the board cannot merely rely on shareholders' approval of the transaction or rely on the market or takeover price to discharge its duties. The board must itself, or through some adviser, obtain the true value or intrinsic value of the shares of the company.[380] Black and Kraakman reiterate this fact by indicating that: "[T]he board planning to sell its company must diligently seek the best price for shareholders."[381] This principle has been recognised in *Revlon case* and it has also been reiterated and refined in a number of cases.[382] The board "is not a passive instrumentality"[383] in the face of takeover and merger transactions. The board may not merely be persuaded by the executive directors without themselves being actively involved and ensuring that they are informed about the merger before asking for shareholder to vote on it.

This decision has been criticised by academics and practitioners alike. It is pointed out that in certain transactions the powers of the board as gatekeepers have been clearly set out in statutes. This will be applicable in transactions such as acquisitions, mergers and assets sales. However, when it applies to tender offers, particularly hostile offers, the role of the board, as a final gatekeeper is not so clearly set out. This is due to the fact that the bidder may directly approach shareholders with an offer.[384] Consequently, there may be a conflict of interest between accountability and authority of the board during tender offers. Directors may be more interested in preserving their positions rather than consider the interests of the shareholders or the company. These potential conflicts of interest have been acknowledged by the courts, hence the need to review the decisions of directors during such transactions. Other scholars

[380] Lederman (2010/2011) *New York Law School Law Review* 649-652.
[381] Black & Kraakman (2002) *North Western University School of Law* 526.
[382] 526.
[383] Bainbridge (2005) *Delaware Journal of Corporation Law* 1.
[384] 2.

indicate that the Delaware courts chose a reasonable balance between avoiding accountability and restricting the board's authority.[385]

Practitioners criticised the approach of the court in this matter, even though they averred that the court achieved the correct result.[386] Critics hold that even though *Van Gorkom* case created a basis to hold directors accountable, the BJR still protects most directors from judicial review both on substantive and procedural grounds. It is asserted that the "probability of a director being found liable for a breach of the duty of care is still incredibly low."[387] This should presumably not discourage directors to take risks for the benefit of the company. Nevertheless, the decision in *Van Gorkom* case, introduced a new era for director's fiduciary duties during a takeover. The decision of awarding damages against directors was novel, and disturbed the business community and the legal fraternity.[388] The decision negatively impacted on the ability of boards to make decisions for fear of personal liability.[389] *Van Gorkom case* had a wide-reaching effect on the conduct of directors in corporate America. Directors reacted in a number of ways including: requesting indemnities; requesting increased cover for liability insurance and being too cautious.[390] Following the decision of the court, the Delaware legislature enacted section 102(b)(7) of the DGCL to deal with these concerns. The section provides:

> "102. Contents of certificate of incorporation
> (a)…
> (b) In addition to the matters required to be set forth in the certificate of incorporation by subsection (a) of this section, the certificate of incorporation may contain any or all of the following matters:
>
> (7) A provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the

[385] See Bainbridge (2005) *Delaware Journal of Corporation Law* 198.
[386] Sharfman (2008) *Delaware Journal of Corporate Law* 301.
[387] Sharfman (November 2006) *The Business Lawyer* 160.
[388] 151.
[389] 151.
[390] Sharfman (2008) *Delaware Journal of Corporate Law* 301-302.

> liability of a director: (i) for any breach of the directors duty of loyalty to the corporation or its stockholders;(ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law;(iii) under s174 of this title; or (iv) for any transaction form which the director derived an improper personal benefit. No such provision shall eliminate or limit the liability of a director for any act or omission occurring prior to the date when such provision becomes effective. All references in this paragraph to a director shall be deemed to refer to such person or persons, if any, who, pursuant to a provision of the certificate of incorporation in accordance with s 141(a) of this title, exercise or perform any powers or duties otherwise conferred or imposed upon the board of directors by this title."

The effect of the section was to eliminate the duty of care in actions against directors for money damages. The charters of Delaware corporations have since been amended to remove such liability to the extent allowed by law.[391]

Scholars indicate that the Delaware corporate law standard of review of directors' duties have rapidly developed over the years. The decisions by courts when reviewing directors' duties have not been without criticism from scholars and practitioners alike. The development of corporate law relating to the standard of review of duties of directors in Delaware, has not been without concerns.[392] Considering the difficulties of the fundamental questions being asked and the speed with which judges are required to make decisions on the new law of corporate mergers and takeovers, it is understandable that courts made imperfect decisions. The courts were required to develop a body of rules to impose legal order upon a new dynamic phenomenon where there were no precedents and no government authority regulating such transactions.[393] The courts then had to employ some doctrine to evaluate the decisions of directors in a multitude of circumstances.

[391]Lederman (2010/2011) *New York Law School Law Review* 640.
[392]Allen *et al* (2001) *Delaware Journal of Corporate Law* 864.
[393]863-867.

It is not surprising that the standards of reviewing directors conduct developed are imperfect.[394] The courts used the BJR to link the disparate standards.[395] The various cases dealing with new standards of review of directors' duties in cases such as *Blasius, Unocal, Revlon* and others, were decided within a relatively short time of each other.[396] Many companies were faced with hostile offers.[397] The courts in those decisions sought to develop a consistent and coherent body of legal doctrine. There was a need for the courts to innovate to deal with new forms of takeovers and board responses thereto. The tools had to be flexible and this made it even more difficult to perfect them.[398] There is a need to adopt mid-course corrections so as to preserve the benefits of those innovations and eliminate their dysfunctions.[399] The decisions dealing with judicial review of directors' duties during takeovers and mergers were taken without due regard to the policies underlying the purpose of applying those standards.[400] There should be a closer alignment between the standards of judicial review used in Delaware corporate law and the underlying policies that that body of law seeks to achieve.[401] It is also suggested that the new standards of review increased in number when a smaller number would have "provided a more coherent analytical framework".[402] It is further suggested that a rigorous functional examination of existing corporate law standards of review will clarify their application, reduce their number, and facilitate the task of corporate advisors and courts.[403] For this purpose there should be three basic standards of review:

> "(i) a gross negligence standard of review for claims that directors are liable for damages caused by their inattention-a standard that would require a plaintiff to prove both a breach of the duty and the fact and extent of any damages caused by the breach;

[394]863-867.
[395]863-867.
[396]867.
[397]865.
[398]866-867.
[399]866-867.
[400]864.
[401]864-867.
[402]864.
[403]864

> (ii) a rehabilitated entire fairness standard to address duty of loyalty claims; and (iii) an intermediate standard of review to govern challenges to director decisions arguably influenced by an entrenchment motive, e.g., the adoption of antitakeover defensive measures or the approval of a change of control." [404]

Scholars argue that these standards will lead to efficiency in formulating the general standards reviewing duties of directors. Standards for reviewing the conduct of directors serves an important policy function. They are intended, among others, to ensure that courts do not erroneously make decisions which may deter directors from risk-taking to the detriment of shareholders.[405] Creation of more standards of review may create a false sense that shareholders are adequately protected.[406] The fact that directors comply with a standard does not necessarily mean that shareholders' interests are better protected. A more functional approach to the standards of review for directors' duties is required.[407] There should be an evaluation of the existing corporate law standards of review so as to clarify their application and, reduce their number so as to facilitate their application by the courts and practitioners.[408] Delaware corporate law has been referred to as being unsettled on two basic issues. These are:

> "[T]he precise reach but also the continuing utility of the business judgment rule as now formulated, and whether a narrow corporate purpose is and should be mandated."[409]

2 6 An overview: Appraisal right in the State of Delaware

The concept of appraisal rights in the US has been in existence for some time. An earlier judicial pronouncement on appraisal rights states that the aim of the

[404]865.
[405]869.
[406]869.
[407]864.
[408]867.
[409]LPQ Johnson "Unsettledness in Delaware Corporate Law: Business Judgment Rule, Corporate Purpose" (2013) 38 *Delaware Journal of Corporate Law* 450.

right is to protect dissenting shareholders.[410] It appears that one of the first cases to refer to an appraisal right is *Lauman v Lebanon Valley Railroad Co,*[411] a case decided during 1858.[412] In the *Lauman case*, the court held that the dissenter could not be forced to accept new shares in the acquirer but the company was forced to pay the dissenter in cash before it could proceed with the merger.[413] The dissenter was paid cash for his shares without the benefit of legislation.[414] The appraisal right is defined as a right that entitles a shareholder opposing certain transactions entered into by a company, to have his or her shares bought by the company in cash at an agreed price or, failing, at a price determined by a court order. No fault is required, and only shareholders who have adhered to the procedural requirements will be entitled to exercise the right. Most states in the US have some form of appraisal right and it is asserted that it has been in existence "ever since the needs of Modern Corporation forced abandonment of the common law requirement of unanimous stockholder authorization for fundamental corporate changes".[415] In the State of Delaware, section 262 of the DGCL provides a basis for shareholders to exercise appraisal rights whenever a fundamental change occurs in the corporation. Section 263 of the DGCL provides for a statutory authority to raise appraisal rights in short-form mergers when a controlling shareholder owns at least 90 percent of the shares in the target company in a cash-out or going-private transaction.[416]

However, their rights are limited. In the matter of *Krieger v Wesco Financial Corp.,*[417] the Delaware Court of Chancery held that shareholders were not entitled to appraisal rights in terms of section 262 of the DGCL, when those shareholders could choose to be paid in shares of an acquirer whose shares

[410] Anderson v International Minerals & Chemical Corporation 67 NE 2d 573 (NY, 1946).
[411] 30 PA 42 1858.
[412] See B Manning "Shareholder's Remedy An Essay for Frank Coker" (1962) 72 *The Yale Law Journal* 230 and discussions under notes 20 and 38 of the article.
[413] See Manning (1962) *The Yale Law Journal* 230 at note 20.
[414] See Manning (1962) *The Yale Law Journal* 230.
[415] LS Daniel "Some Observations on the Scope of Appraisal Statutes" (1958) *The Business Lawyer* 240-253 240.
[416] ZA Paiva "Ouasi-Appraisal: Appraising Breach of Duty of Disclosure Claims following "Cash-Out" Mergers in Delaware" (2017) 23:1 *Fordham Journal of Corporate & Financial Law* 243.
[417] C.A. No. 6176-VCL (Del. Ch. Oct. 13, 2011).

were publicly traded.[418] Section 262(g) of the DGCL has recently been amended to limit appraisal right demands by including a *de minimis* exception. This amendment restricts appraisal demands where the value or number of shareholders' shares is minimal. The *de minimis* restriction is applicable only to shares listed on a national exchange immediately before the transaction.[419] Delaware's state law does not allow appraisal rights for shareholders where there is an asset sale by the company or an amendment of certificate of incorporation under section 242 of the DGCL.[420]

There are four main questions regarding the basic application of the appraisal remedy. These are: what kinds of transactions support appraisal rights; what are the procedural requirements for enforcement of the appraisal rights; how do courts determine "fair value" in appraisal rights; and, is the appraisal right the only remedy available to dissenting shareholders.[421] The appraisal right allows for a balance between the needs of the majority to vote on certain transactions and the minority whose shares may be negatively affected. Minorities are afforded an opportunity to disinvest on fair and reasonable terms. It is generally accepted that bringing an appraisal rights action can be quite complex.[422] The fact that the exercise of appraisal rights is subject to a number of detailed and complex procedures does not assist the applicant in obtaining an appraisal remedy. It appears that failure to comply with one of these steps may jeopardise the ability to exercise such a right. The Delaware appraisal section is one of the most limited of state codes.[423] Costs of raising appraisal rights may run into millions and the shareholder is not certain of a successful outcome.[424] Appraisal rights are controversial and are continually being reviewed.[425] Appraisal rights introduced in terms of section 164 of the Companies Act of 2008 are discussed in chapter 5 6 6 below.

[418] C.A. No. 6176-VCL (Del. Ch. Oct. 13, 2011).
[419] Paiva (2017) *Fordham Journal of Corporate & Financial Law* 244.
[420] Oesterle *The Law of Mergers and Acquisitions* 98.
[421] 98.
[422] 115.
[423] 98.
[424] 102.
[425] 99.

2 7 Concluding remarks

One of the important reasons for the courts to closely consider decisions of directors is that takeovers or mergers increase conflict of interest among directors. This concern is reasonable. Directors may be faced with job losses and loss of perks after the takeover or merger. Therefore, directors may be influenced by ulterior motives when considering a takeover or a merger. It is generally acknowledged that directors know more than shareholders about the business of the companies in which they preside. By virtue of this knowledge they also understand to what extent a takeover or a merger will be to the benefit of the bidder and the target company. In addition, statutory mergers cannot be completed without the co-operation of the board.[426] However, these can also result in conflicts of interest. The bidder knows that statutory merger transactions can only be voted on by shareholders after approval and recommendation by the board of directors. This may encourage the bidder to compensate the directors to ensure their co-operation. This can lead to side payments for directors.[427] Hence there is a need for vigilance and enhanced scrutiny of such transactions. The role of the independent board members plays a crucial role during this period. Acquisitions give rise to any number of managerial agency problems. Board independence may control these concerns better.[428]

The Delaware courts try to establish a balance between authority and accountability when they assess the fiduciary duties of directors.[429] The board has legitimate authority to approve, recommend approval or prevent a merger. The courts closely scrutinise the role of the board during a takeover or merger. It will examine the extent to which they were advised of the mergers, the relevant information they had prior to their decision to merge, and the extent to

[426]See discussions under paragraph 2 4 1 above.
[427]Bainbridge (2013) *Fordham L. Rev* 3288- 3289.
[428]JN Gordon "The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices" (2007) 59 *Stanford Law Review* 1465*. Columbia Law and Economics WP No. 323*. 1503. Available at: SSRN: https://ssrn.com/abstract=10863797, (Accessed 20-11-2017).
[429]Bainbridge (2005) *Delaware Journal of Corporation Law* 198.

which they were independent of any influence by incumbent management. The State of Delaware has established itself as the preferred state for registration of companies.[430] Further it is generally accepted that the Delaware courts have created some of the important principles relating to takeovers and mergers.[431]

The standards of reviewing the conduct of directors during takeovers and mergers are some the important principles created by the Delaware courts.[432] These principles are also extended beyond takeover law and are useful as a measure of how directors have exercised their fiduciary duties in their day-to-day business operations. The appraisal remedy in Delaware raises a number of concerns and is continuously reviewed by the courts, and recently, by the Delaware State Legislature through an amendment.[433] It is acknowledged that the appraisal right is complex and its effect uncertain. Its efficacy in protecting shareholders has been questioned. Furthermore, as indicated in the *Unocal case,*[434] Delaware corporate law is not static, it grows and develops in response to needs and evolving corporations and their operating environment. This is supported by Anabtwi who argues that certain standards of reviewing conducts of directors such as the enhanced scrutiny created in the *Unocal case* and the review of sale of control in *Revlon case* have reached their twilight due to erosion and relaxation of their application over time.[435]

The adoption of certain provisions from US corporate law under the South African Companies Act of 2008, such as the appraisal rights in section 164 and statutory mergers in section 113, will require that some of the principles established by the State of Delaware's judiciary will in future play an important role in the interpretation of these sections. This promotes development of takeovers and merger law in South Africa, to better serve investors and shareholders. Practitioners and academics alike would welcome this development of SA company law. However, two important limitations of this

[430]Introduction to this chapter 2.
[431]See paragraph 2 5 above
[432]See paragraph 2 5 above.
[433]See Paiva (2017) *Fordham Journal of Corporate & Financial Law* 243.
[434]493 A.2d 946 (Del. 1985).
[435]Anabtawi (January 2019 Forthcoming) *Delaware Journal of Corporate Law* 43.

approach should be borne in mind. The continuous mutation of Delaware law requires that SA laws must also be continuously monitored and adjusted to ensure alignment with new developments. Moreover, caution is required when adopting principles from Delaware, as that judicial system and the economy under which its corporation laws are applied are significantly different from those in South Africa.

Chapter 3: An overview of the application of the mandatory offer rule in the United Kingdom

"The mandatory bid rule is one of the most discussed rules that Member States had to implement. The mandatory bid rule aims to provide the minority shareholders with the opportunity to exit the firm on fair terms, but arguably fails to open up the market for corporate control."[1]

3 1 Introduction

The enforcement of the mandatory offer requirement forms one of the cornerstones of the powers of the UK Takeover Panel. The mandatory offer has also been extended to a number of EU countries in terms of the Takeover Directive.[2] This has increased the debates surrounding the desirability of such a rule in a number of EU countries.[3] This chapter deals with regulation of mandatory offers in the UK. It is important to understand how the mandatory offer rule developed in England before attempting to discuss its application in South Africa. This may assist in establishing the rationale for applying the requirement in South Africa, despite the apparent different economic and financial market structures of both countries.

As mentioned in Chapter 1, the rationale behind choosing the UK as a comparative jurisdiction is that South African company law is based mainly on

[1]JA McCahery & E Vermeulen "Does the Takeover Bids Directive Need Revision?" (2010) *Tilburg University, Tilburg Law and Economic Center* 7.
[2]Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on Takeover Bids (Takeover Directive). However, it must be noted that some, EU countries may choose to opt out of the mandatory offer rules. Member states may also tailor-make certain provisions for their own countries.
[3]See P Bockli, P Davies, E Ferran, G Ferrarini J Garrido Garcia, K Hopt, A Pietrancosta, K Pistor, R Skog, S Soltysinski, J Winter and E Wymeersch, European Law Experts "Response to the European Commission's Report on the Application of the Takeover Bids Directive" (2014) *University of Cambridge Faculty of Law Legal Studies*. Paper No.5/2014 3. Available http://www.law.cam.ac.uk/ssrn (Accessed 20-3-2014).

English company law.[4] In addition, the most important section dealing with mandatory offers in South Africa, section 123 of the Companies Act of 2008, and the Takeover Regulations are based on the UK City Code on Takeovers and Mergers (the City Code). The predecessor to section 123, rule 8 of the Securities Regulation Code on Takeovers and Mergers and the Rules of the Securities Regulation Panel, were also based on the City Code. [5]

3 2 The development of the mandatory offer in the United Kingdom

3 2 1 A brief overview of developments leading to the mandatory offer

The mandatory offer requirement is one of the strongest expressions of the equality rule in takeovers and mergers.[6] The mandatory bid rule is also known as the Equal Opportunity Rule.[7] The equal opportunity rule as expressed in *Perlman case* has been discussed in paragraph 2 2 above. There are a number of interlinked principles for the enforcement of the mandatory offer in takeovers. Scholars assert that after a change of control, the future hopes and interests of the shareholders lie with the new controlling shareholder.[8] Minority shareholders of the controlled company can be prejudiced should the new controlling shareholder not conduct the affairs of the company properly.[9] Once there is a change of control of a company, shareholders must be given an opportunity to leave the company and sell their shares to the new controlling shareholder on the same terms as those who sold theirs to the new controlling shareholder. The opportunity to sell should not be dependent on the willingness

[4]HS Cilliers, ML Benade, JJ Henning, JJ Du Plessis & PA Delport *Corporate Law* 2nd ed (1992) 16; See also S Luiz An *Evaluation of the South African Securities Regulation Code on Takeover and Mergers* LLD thesis Unisa (2003) 6.
[5]This is indicated in the Explanatory note of the Securities Regulation Code and Mergers and the Rules of the SRP Code. The SRP Code indicates that it is based mainly on the City Code on Takeovers and Mergers, which has been issued by the London Panel on Takeovers and Mergers. See also Luiz *An Evaluation of the South African SRP Code* (2003) 573-1022.
[6]PL Davies, & S Worthington Gower *Principles of Modern Company Law 10th ed* (2016). 962..
[7]See RA Albuquerque & E J Schroth "Determinants of the Block Premium and of Private Benefits of Control" (2008) *ECGI Finance Working Paper No.202/2008 and Swiss Finance Institute Research Paper No. 08-21.* 2.Available at SSRN:
https://ssrn.com/abstract =1099901, (Accessed 21-2-2018).
[8]Davies & Worthington *Gower Principles of Modern Company Law* 968-969.
[9]968-969.

of the new controlling shareholder to voluntarily make a general offer, but should instead be compulsory.[10] The essence of the mandatory offer requirement is contained in two principles: Firstly, shareholders should have the opportunity to sell and exit the company whose control has changed,[11] and secondly, the shareholders should have the opportunity to sell their shares on the same terms as those who sold theirs to the new controlling shareholder. [12] The latter requirement is the most controversial.[13]

It appears that the mandatory offer requirement developed alongside rules relating to disclosures in respect of takeovers and mergers. This makes sense as companies seeking funds are also subject to disclosure rules to ensure that investors are protected. Accordingly, when there is a disinvestment, or sale of shares particularly by a major shareholder, similar rules should also apply. The initial rules to regulate takeovers and mergers appears to have been aimed at preventing fraud and misleading information during takeovers. It appears that in earlier times there were few measures to protect investors during takeovers and mergers. One the statutory provision was the Prevention of Fraud (Investments) Act of 1958.[14] An offer document is an invitation to the offeree shareholders to dispose of their shares, therefore, it falls within the statutory regulation of investment circulars imposed by this Act.[15] Possibly due to an attempt to mainly prevent fraud and misinformation, authorities saw fit to regulate disclosures in respect of takeovers and mergers, as it was believed that more disclosures would promote protection for investors, particularly minority shareholders. It was assumed that more disclosures would assist investors in making an informed decision about their investments. Prior to the introduction of these regulations, changes-of-control transactions were marked by poor disclosures. This increased the risk that investors could be treated

[10]968-969.
[11]968-969.
[12]968-969.
[13]969.
[14]See Prevention of Fraud (Investments) Act of 1958, CHAPTER 45. UK General Acts. Available on: http://www.legislation.gov.uk/ukpga/1958/45/section/26/enacted. Accessed 20.2.2019.The Act created offences for certain conduct when dealing in securities. These included providing false and misleading information.
[15]RR Pennington Penningtons'Company Law (1980) 805.

unfairly and that minority shareholders could be oppressed by the majority. The Bank of England had, before the formal regulation of takeovers, also been instrumental in introducing more protective measures for investors in respect of mergers and takeovers.[16]

A review of the literature suggests that the rules relating to the regulation of takeovers and mergers underwent a number of developments over a long period of time as regulators sought an effective regulatory regime to protect investors Methods to acquire control of companies had to be developed by practitioners as the need for takeovers developed. Regulators on the other hand had to improve their methods of protecting shareholders. In the UK, schemes became operative in the 1960[17] These schemes of arrangement then developed into a procedure for the takeover of a company by which the squeeze out provisions could be avoided.[18]

The UK developed quasi-self-regulatory procedures for takeovers long before statutory regulation was established in other European countries.[19] The origin of takeover regulation can be traced back to a period between 1950 and 1960, when bidders took advantage of the lack of regulation of mergers.[20] Takeovers were regarded as “sharp practice” at that time and some directors and authorities believed that they were harmful to companies and investors alike.[21] Possible abuse and unfair treatment of investors during the takeover frenzy spurred regulatory authorities into action.

In the development of any new industry there is bound to be opportunists who may easily take advantage of inadequacies in existing laws. Hence, there was

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[16]See Armour et al ‘The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework (2011) Vol 52 *Harvard International Law Journal* 235 also FB Palmer & CM Schmitthoff *Palmer’s Company Law* 24 ed (1987) 1178 and Luiz *An Evaluation of the South African SRP Code* Vol. 1: 13.
[17]Luiz ‘Some comments on the regulation of takeovers and mergers’ (1997) 9 *SA Merc Law Journal* 240.
[18]Luiz (1997) *SA Merc Law Journal* 240.See Luiz *An Evaluation of the South African SRP Code* Vol. 1: 15.
[19]Davies & Worthington *Gower Principles of Modern Company Law* 920.
[20]920
[21]L Gullifer & J Payne *Corporate Finance Law Principles and Policy* (2011) 568.

a need to formulate new rules to cater for these developments. New complex methods of achieving takeovers and mergers attracted the attention of financial services authorities that were concerned about possible abuse. The increasing, and often controversial, burgeoning takeover and merger practices led to the development of regulation of takeovers and mergers.[22] Protective measures for investors were required as bidders took advantage of the absence of regulatory oversight.[23] These concerns resulted in the introduction of the Queensberry Rules in 1959, which were modest rules.[24] These rules or guidelines, titled "Notes on Amalgamation of British Businesses", were brief but did establish the principles relating to shareholder primacy in the regulation of takeovers. The guidelines then formed the core principles in English law for regulation of takeovers.[25] The guidelines emphasised that there should be no interference with the free market for shares, that shareholders should decide for themselves whether to sell or not. Further, shareholders were to be given enough time and sufficient information in order to make informed decisions about takeover offers.[26] Lack of adjudication and enforcement procedures for these guidelines eventually led to their undoing, even though they were well received.[27] Their perceived ineffectiveness led to hostile criticism in the financial media and there were calls for a more determined body to police takeovers.[28] In addition, the UK government entered the fray with veiled threats that if the industry could not, or does not introduce its own effective regulatory and enforcement methods, then the Government would intervene.[29]

Regulation of takeovers and mergers in the UK developed through a number of phases.[30] Hostile takeovers and changes to share ownership also emerged

[22]B Rosenzweig "Private Versus Public Regulation: A Comparative Analysis of British And American Takeover Controls" (2007) 18 *Duke Journal of Comparative & International Law* 224.
[23]Davies & Worthington *Gower Principles of Modern Company Law* 920.
[24]920
[25]Gullifer & Payne *Corporate Finance Law Principles and Policy* 568.
[26]568.
[27]568.
[28]D Prentice "Take-over Bids – The City Code on Take-over and Mergers" (1972) 18 *McGill LJ* 18:3. 386.
[29]Prentice (1972) 18 *McGill LJ* 18:3. 386-387.
[30]See Davies & Worthington *Gower Principles of Modern Company Law* 920-921.

through various stages.[31] The development of the mandatory offer requirement in the UK appears to have been spurred by the rapid increase of merger and takeover transactions, which resulted in a number of "squabbles in contests for control of public companies." [32] It is also evident from the literature reviewed that these developments were partly due to the inability of regulators to find regulatory procedures which could cater for the conflicting interests of shareholders, supervisory authorities and companies.[33] The continuing changes in the investment environment, as companies and practitioners introduced additional takeover methods such as partial offers had the effect that the regulations which were previously adequate to prevent a negative impact on minority shareholders, became inadequate.[34] The introduction of new takeover methods such as leveraged takeovers by private equity funds also made discussions on regulation of takeovers more relevant.[35]

It is arguable that the introduction new takeover methods could not be properly regulated under the same regulations. Hence, there was a need for regulators to keep improving their regulations to ensure that they stayed up to date with new developments in financial markets.[36] The then 'Notes' were not adequate to deal with developments of defensive measures in takeovers. The courts resolved the disputes using common-law fiduciary duties.[37] The approach was not acceptable to investors due to the delays it caused and uncertainty in the transaction. The delays made reduced the likelihood that takeovers would succeed and litigation as a defensive measure was also potent.[38]

[31]Johnston (2007) *Cambridge Law Journal* 423.
[32]See Prentice (1972) *McGill LJ* 385 and also Johnston (2007) *Cambridge Law Journal 435-436.*
[33]See Prentice (1972) *McGill LJ* 385-386 and 416-417.See also Johnston (2007) *Cambridge Law Journal* 422-442
[34]See Johnston (2007) *Cambridge Law Journal* 444-445.
[35]Johnston (2007) *Cambridge Law Journal* 460.
[36]436.
[37]436.
[38]436.

3 2 2 *The Panel on Takeovers and Mergers and the City Code on Takeovers and Mergers*

Following criticism and concerns raised, the elaborate City Code was introduced. It forms the basis of the current City Code.[39] The introduction of the City Code effectively stemmed litigation during takeovers.[40] The City Code was established and promulgated as a self-regulatory body of rules in the UK in 1968.[41] A community of institutional investors and investment bankers drove the making of the rules forming the City Code.[42] With the publication of the City Code, the Panel on Takeovers and Mergers was also created to administer and enforce this regulatory document.[43] Regulation of takeovers and mergers in the UK appears to have been driven by the need to protect shareholders, and no other stakeholders, as can be seen from the following statement by Hinton:[44]

> "[W]e see the lead constituent as far as the book is – the takeover panel is concerned as being the shareholder, they are the only people in a bid who have an investment decision to make and so we think they're the people who deserve some protection..."

Originally, the UK Panel was not based on statute.[45] This fact could easily lead to underestimation of the powers of the UK Panel.[46] In R v *The Panel on Takeovers and Mergers, ex parte Datafin plc. and another* (*Datafin case),* [47] it

[39]See Prentice (1972) *McGill LJ* 387.
[40]Johnston (2007) *Cambridge Law Journal* 441.
[41]UK City Code in the Introduction 12th Ed (2016). See also H Baum "Takeover Law in the EU and Germany: Comparative Analysis of a Regulatory Model" (2006) 3 *University of Tokyo Journal of Law and Politics* 2.
[42]JA Armour & DA Skeel Jr. "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of US and UK Takeover Regulation" (2007) 95 *The Georgetown Law Journa*l, 1727.
[43]Davies & Worthington *Gower Principles of Modern Company Law* 920
[44]N Hinton, Former Deputy Director General of the Panel, South African Corporate Law Reform Roundtable Meeting held in England 19 March 2005.
[45]Davies *& Worthington Gower Principles of Modern Company Law* 920, see also the City Code 12th ed (2016), Introduction.
[46]See Davies & Worthington *Gower Principles of Modern Company Law* 920.
[47]1987 QB 815 CA.

has been described as "a truly remarkable body…. performing this function without visible means of legal support."[48] The court further indicated as follows:

> "[L]acking any authority *de jure* it exercises immense power de facto by devising, promulgating, amending and interpreting "The City Code on Take-over and Mergers", by waiving or modifying its application of the Code in particular circumstances, by investigating and reporting upon alleged breaches of the Code and by the application of sanctions. These sanctions are no less effective because they applied indirectly and lack a legally enforceable base."[49]

The UK Panel has been closely associated with the London Stock Exchange.[50] This may explain its efficacy as co-operation between the institutions promote shareholder protection. The promulgation of the EU Takeover Directive[51] has since required that the UK Panel change its status to a statutory body. The new statutory regime has also been designed with the clear objective of maintaining the earlier self-regulatory regime.[52] Even though the City Code is now on a statutory basis, it should on balance be considered to be a self-regulatory instrument.[53]

The statutory basis of the Panel is set out in terms of chapter 1 of part 28 of the UK Companies Act 2006.[54] The role and function of the Panel and the City Code, however, still remain largely unchanged.[55] The Panel still retains its status as a regulator of takeovers and composition of its members has not been affected by the changes brought about by the UK Companies Act 2006. Members of the Panel and its various committees come from various professions including: banking, investment banking, pension funds, chartered accountancy and the legal professions.[56] The composition of the panel

[48] 1987 QB 815 CA.
[49] 1987 QB 815 CA.
[50] See Palmer & Schmitthoff *Palmer's Company Law* 82-02.
[51] Directive on Takeover Bids (2004/25/EC).
[52] Gullifer & Payne *Corporate Finance Law Principles and Policy* 568.
[53] Johnston (2007) *Cambridge Law Journal* 447.
[54] See UK Companies Act 2006, sections 942-965.
[55] Gullifer & Payne *Corporate Finance Law Principles and Policy* 572.
[56] See Introduction to the City Code.

indicates the various commercial interests operating in the UK.[57] The UK Panel has also retained its rule-making and adjudication functions, where it gives rulings and enforces compliance with the City Code.[58]

The UK Companies Act 2006 created new powers for the Panel. It can now also require parties to disclose information that it reasonably requires to exercise its powers and functions.[59] The Panel may enforce the City Code by issuing rulings relating to compensation of parties,[60] and rulings in respect of compliance.[61] It also has the power to discipline parties who are subject to the rules of the City Code.[62] The City Code has a wider remit than the Takeover Directive. [63]

The UK Panel may still sanction the parties as it did prior to the implementation of the Takeover Directive.[64] Sanctions include a private reprimand, a public censure and a request that institutions represented on the Panel withdraw facilities from the securities market.[65] This is commonly known as 'cold-shouldering'[66] and refers to the denial of various services or funding to a party who is alleged to have breached rules of the City Code. It is suggested that the sanction of 'cold-shouldering' plays an important role as one of the enforcement measures of the Panel. This type of sanction appears to be unique to the UK

[57]See Prentice (1972 *McGill LJ* 387.
[58]Gullifer & Payne *Corporate Finance Law Principles and Policy* 572.
[59]UK Companies Act 2006 section 94; See also Gullifer & Payne *Corporate Finance Law Principles and Policy* 572.
[60]UK City Code in 10 (c), Enforcing the Code.
[61]UK City Code in 10 (d), Enforcing the Code.
[62]UK City Code in 11, Powers to discipline parties who have transgressed the City Code.
[63]Gullifer & Payne *Corporate Finance Law Principles and Policy* 572.
[64]573.
[65]572.
[66]See Takeover Appeal Board "Principle Capital Investment Trust PLC- Decision of the Appeal Board" (2010) 14 www.the takeoverappealboard.org.uk (Accessed 20-12-2013) A ruling of The Appeal Board of the Takeover Panel in the matter of Principle Capital Investment Trust Plc (PCIT). 2010/1. In this matter, the directors of PCIT were cold-shouldered by the Hearings Committee of the Panel for a period of 3 years. This was due to their attempt to hide their dealings in shares and misleading the Executive of the Panel in the share dealings to avoid the mandatory offer requirements in rule 9 of the City Code. The parties appealed against the ruling of the Hearing Committee. The Appeal Board confirmed the ruling and indicated that the cold-shouldering and the period is the appropriate sanction taking into consideration the gravity of the transgression, both the sanction and the period of the sanction was justified. Accordingly, the appeal of the directors of PICT was dismissed.

Panel. In addition, the co-operation between the Panel and the Financial Services Authority also bolsters the enforcement powers of the Panel. The Financial Services Authority Handbook, Market Conduct, in section 4.3 supports the sanction of 'cold-shouldering' by providing as follows:

> "A firm must not act, or continue to act, for any person in connection with a transaction to which the Takeover Code applies ... if the firm has reasonable grounds for believing that the person in question, or his principal, is not complying or is not likely to comply with the Takeover Code." [67]

The decisions of the Panel are subject to review by the courts in appropriate cases.[68] The courts have indicated that their role should only be to consider reviewing the decision of the Panel after the takeover has been completed.[69] The courts recognise that takeover proceedings must be completed as speedily as possible and that any intervention has the potential to disrupt the takeover. This approach by the courts has the effect of discouraging would-be litigants intending to delay a takeover. Tactical litigation is accordingly discouraged.[70]

The review power of the courts is used in line with the judgment of the *Datafin case.*[71] In that case, the court indicated that:

> "It is not for a court exercising a judicial review jurisdiction to substitute itself for the fact-finding tribunal, and error of law in the form of a finding of a fact for which there was no evidence or in the form of a misconstruction of the panel's own rules would normally be a matter to be dealt with by a declaratory judgment. The only circumstances in which I would anticipate the use of remedies of *certiorar*i and mandamus would be in event, which I hope unthinkable, of the Panel acting in breach of the rules of natural justice, in other words, unfairly. Nothing that I have said fetter or is intended to or should be construed as fettering the discretion of any court to which application is made

[67] Rosenzweig (2007) *Duke Journal of Comparative and International Law* 213.
[68] LS Sealy & S Worthington *Sealy's Cases and Materials in Company Law* 9 ed (2010) 714.
[69] [1987] QB 815; See also *R v The Panel on Takeovers and Mergers, ex parte Guinness plc* [1990] 1QB 146.
[70] J Mukwiri "The myth of tactical litigation in UK takeovers" (2008) 8 :2 *Journal of Corporate Law Studies* 373-388.
[71] 1987 QB 815 CA.

for leave to apply for judicial review of a decision of the panel or which leave having been granted, is charged with the duty of considering such an application. Nevertheless, I wish to make it clear beyond a peradventure that in the light of the special nature of the panel, its functions, the market which is operating, the time scales which is inherent in that market and the need to safeguard the position of their parties, who may be numbered in thousands, all of whom are entitled to continue to trade on an assumption of the validity of the panel's rules and decisions, unless and until they are quashed by the court, I should expect the relationship between the panel and the court to be historic rather contemporaneous. I should expect the court to allow contemporary decisions to take their course. Considering the complaint and intervening, if at all, later and in retrospect by declaratory orders which would enable the panel not to repeat any error and would relieve individuals of the disciplinary consequences of any erroneous finding of breach of the rules. This could provide a workable and valuable partnership between the courts and the panel in the public interest..."[72]

The court in the *Datafin* case[73] indicated that this is due to the special nature of the function of the Panel. It is required that market integrity be maintained, the timelines set in the City Code rules be observed, and that parties who deal on the basis of decisions of the Panel continue to rely on those decisions. The courts will grant relief in the form of a declaratory order after the event and will not interfere with the panel's regulatory process during a takeover.[74] Therefore, based on this approach, the courts will only give guidance to the panel after the takeover has been completed. This is with a view to ensuring that a similar error should not occur.[75]

The decision in the *Datafin* case has been followed in *R v Panel on Takeovers and Mergers, ex parte Guinness plc.*[76] In the *Guinness* case, the court indicated

[72][1987] QB 815 CA. 842.
[73][1987] QB 815.
[74]Sealy & Worthington *Sealy's Cases and Materials in Company Law* 715. In the commentary, it is suggested that the courts do not interfere with takeover process.
[75]Mukwiri (2008) *Journal of Corporate Law Studies* 373-388.
[76][1990] 1 QB 146, CA. See also comments by Sealy & Worthington *Sealy's Cases and Materials in Company Law* confirming that the UK courts readily accept the UK Panel as the appropriate forum for regulating takeovers.

that during a takeover process the time-lines are short and it is important that financial-markets participants should be able to rely on rulings of the Panel. Therefore, the intervention of the courts may not be possible, or may even be against public interest.[77] In another case of *R v Panel on Takeovers and Mergers, ex parte Fayed,*[78] a case involving the disciplinary powers of the UK Panel, the court emphasised the importance of the Panel in regulating takeovers and mergers. In that case, the court also refused to intervene during the course of a takeover. The court referred to the earlier decision in *Datafin and Guinness Plc* cases. [79]

The City Code is divided into: the introduction, the general principles, the definitions and the rules. In addition, the rules have detailed explanatory notes for some rules and also appendices on certain rules.[80] The UK Panel has a number of committees.[81] Nominating organisations are entitled to designate members for different committees and may also have alternate members.[82]For the purposes of the dissertation the following are relevant. The Code Committee, as the name implies, is mainly responsible is to keep the City Code updated by ensuring that the rules are amended as when it is required. The Hearings Committee is responsible for reviewing rulings of the Executive and conducts disciplinary hearings for breach of the City Code.[83] Rules of procedures of the Hearings Committee are set out in Appendix 9 to the City Code. Membership of the Panel's committees is restricted. For instance, members are only allowed to be on one committee. No person who is or has been a member of the Code Committee may simultaneously or subsequently be a member (or an alternate of a member) of the Hearings Committee or the Takeover Appeal Board (Appeal Board).[84]

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[77][1989] 1 All ER 509, 512.
[78][1992] BCLC. 938.
[79][1992] *BCLC* 938.
[80]The UK City Code.
[81]See UK Panel website. http://www.thetakeoverpanel.org.uk/structure/committees.The other committees are for administrative purposes and corporate governance matters.
[82]See UK City Code in 4(a) of the introduction.
[83] See 4 of the introduction to the UK City Code.
[84]See 4 (a) to (d) of the introduction the UK City Code.

When the Panel acts in relation to any proceedings before the Hearings Committee or the Appeal Board, it must do so only by an officer or member of staff (or a person acting as such) who must not be a member of the Code Committee, the Hearings Committee or the Board.[85] The restriction appears to be aimed at separation of responsibilities within Panel committees. This ensures independence between committees and prevents members of the Code Committee adjudicating and interpreting rules as members of the Hearings Committees. The rules of the Appeal Committee are available on its separate website and are also briefly referred to in the City Code.[86]

The self-regulatory model may not be the solution for other jurisdictions as the success of the model is dependent on the specific parties involved in the regulatory system.[87] One of the distinguishing features of the UK Panel is the ability to apply the rules in a flexible and informal manner. It is therefore doubtful that a formal government body could play a similar effective role. Government regulation has a tendency to become rigid and bureaucratic.[88] Despite the UK Panel's metamorphosis from self-regulatory to a statutory footing, its status and roles remained mainly unaffected.[89] Therefore, it could be argued that the effectiveness of the regulatory system is closely tied to the incentives of the individuals and entities that provide the rules.[90]

3 2 3 The application of the mandatory offer rule in the United Kingdom

The mandatory offer rule is closely linked to the equal opportunity rule as already discussed above in chapter 2. The mandatory offer rule was originally introduced in the UK City Code as rule 35 during 1972. The initial threshold was acquisition of 40 percent of the issued shares.[91] The rationale for setting a

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[85]See 8 of the introduction to the UK City Code.
[86]See 8 of the introduction to the UK City Code. The Appeal Board rules are available at: www.thetakeoverappealboard.org.uk. (Accessed 15 -08-2017).
[87]Amour & Skeel Jr. *(*2007) *Georgetown Law Journa*l 1785.
[88]See Prentice (1972) *McGill LJ* 414-415.
[89]Gullifer & Payne *Corporate Finance Law Principles and Policy* 573. See also Amour & Skeel Jr. *(*2007) *George Town Law Journal* 1788.
[90]See Armour & Skeel Jr. (2007) *George Town Law Journal* 1785.
[91]Prentice (1972) *McGill LJ* 392.

specific threshold solved the problem of having to define control for the purpose of the rule. It is acknowledged that defining control is not easy due to the fact that it involves a number of variables including, whether a company has a dispersed shareholding and shareholder participation in the affairs of the company.[92] The mandatory offer rule was originally applied only where effective control was acquired from company officers. The UK Panel determined what constituted acquisition of control on a case-by-case basis.[93] However, it has become common to set specific thresholds to determine control for the purpose of the mandatory offer in most countries. The mandatory offer rule is triggered at various shareholding levels in various countries. Countries introduce different thresholds taking into consideration, among others, the size of companies and type of shareholding in those companies.[94] There are no studies that show the optimal ownership levels at which a mandatory offer must be made. This results in different mandatory offer thresholds throughout the world, ranging from an acquisition of 15 percent of the shares in India to an acquisition of 67 percent shares in Finland.[95] The 30 percent voting rights threshold in the UK has been determined on the basis that in most cases, acquisition of voting rights equivalent to that percentage will constitute effective control.[96] Setting a specific percentage has also created certainty for acquirers and avoids arbitrary determination of control after the fact.

The mandatory offer rule in the UK is in rule 9 of the City Code.[97] The rule includes explanatory notes under each sub-rule. In short, rule 9.1 of the City Code provides that any person who acquires, whether by a series of transactions over a period of time or not, an interest in shares which (taken together with shares in which persons acting in concert with him are interested) have voting rights of 30 percent or more of the voting rights of a company; or any person, together with persons acting in concert with him, is interested in

[92]Prentice (1972) *McGill LJ* 388.
[93]R Skog "Does Sweden need a Mandatory Bid Rule? A Critical Analysis" (1997) *Societe Universitaire Euopeenne de Recherches Financieres (*SUERF*)*. 5
[94]T Nenova "Takeover Laws and Financial Development" (2006) *World Bank Policy Research Working Paper* 4029. 9.
[95]9.
[96]Skog (1997) *Societe Universitaire Euopeenne de Recherches Financieres* (SUERF) 5.
[97]See Annexure Rule 9 of the UK City Code

shares which in aggregate vote between 30 percent and 50 percent of the voting rights of a company acquires an interest in any other shares which increases the percentage of shares carrying voting rights in which he is interested, such person or persons must make an offer to the holders of any class of equity share capital, whether voting or non-voting, and also to the holders of any other class of transferable securities carrying voting rights. The rule has two trigger points for the mandatory offer obligation: acquisitions of 30 percent or more of the voting rights and acquisition of any percentage of voting rights in cases where the acquirer already holds more than 30 percent of the voting rights but not more than 50 percent of the voting rights of a company. This is also referred to as the creep rule. “Creeping in” happens when a bidder holding less than 30 percent makes a voluntary offer to acquire a small percentage of shares at a low price to avoid triggering the mandatory offer. “Creep on” occurs when a shareholder has acquired shares exceeding 30 percent and increases its shares by buying more shares without any legal obligation to make a mandatory offer.[98] Unless the Panel consents otherwise, each person or persons who acquires shares as described above, must make a mandatory offer.[99] The Panel may relax the strict application of the rule in limited circumstances. The mandatory offer rule in the City Code is long and not easy to read. It is suggested that this is due to the fact that the rule is drafted to be as broad as possible to prevent circumvention.

The only condition to the mandatory offer is acceptances in respect of the shares that will result in the acquirer holding more than 50 percent of the voting rights of the company.[100] The payment to be offered must be in cash or be accompanied by a cash alternative at not less than the highest price paid by the offeror, or any person acting in concert with it, for any interest in shares of that class during the 12 months prior to the announcement of that offer. The Panel may also determine the highest price to be paid in appropriate

[98]Böckli, et al (2014*) University of Cambridge Faculty of Law Legal Studies*. Paper No.5/2014. 9-10.
[99]See first sentence to Rule 9 of the UK City Code.
[100]Rule 9.3 of the UK City Code.

circumstances.[101] The City Code prevents voluntary acquisitions unless the acquirer is able to acquire more than 50 percent of the target.[102] This is intended to encourage bidders to make a fair offer, otherwise the bid will fail as more than 50 percent of the shareholders are unlikely to accept an unfair offer price. This prevents bidders acquiring companies ''on the cheap''.[103] In addition, the requirement is intended to put beyond doubt the identity of the *de jure* controlling shareholder.[104] This creates certainty to shareholders as to the identity of the controlling shareholder. Shareholders may then choose to remain invested in the company where they know the identity of the controlling shareholder or may choose to exit their investment where they do not know the controlling shareholder.

The City Code also creates obligations for directors or their related parties when they sell their shares or interests in shares. Such directors must ensure that as a condition of the sale of their shares, the buyer undertakes to fulfill his obligations under the mandatory offer rule. Such persons may also not resign from the board until the first closing date of the offer or the date when the offer becomes wholly unconditional; whichever is the later, unless the Panel agrees.[105] Persons who have an obligation to make a mandatory offer may avoid such an obligation, with the consent of the Panel, by disposing the shares that triggered the obligation. Such persons may not exercise any votes attaching to such shares pending their disposal.[106]

The Panel has wide discretion to dispense with the requirement for a mandatory offer in various circumstances.[107] The mandatory offer may be waived by vote of independent shareholders of the offeree company when the company issues

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[101]Rule 9.5 of the UK City Code.
[102]Rule 10 of the UK City Code.
[103]See E Wymeersch "A New Look at the Debate About the Takeover Directive (2012) Ghent University, Financial Law Institute Working Paper No 2012-05. 7.Available at SSRN: https://ssrn.com/abstract=1988927.(Accessed 20 -5-2018).
[104]See Böckli, el al (2014) *University of Cambridge Faculty of Law Legal Studies*. Paper No.5/2014. 9-10.
[105]Rule 9.6 of the UK City Code.
[106]Rule 9.7 of the UK City Code
[107]See 2(c) in the introduction to the UK City Code.

new securities.[108] The issue of the new securities should be as consideration for an acquisition or a cash subscription. The requirement for a general offer will also be waived, provided there has been a vote of independent shareholders, in cases involving the underwriting of an issue of shares which results in the underwriter crossing the 30 percent threshold. This could be due to the company not having sufficient underwriters to subscribe for the issue of shares.[109] The issue of shares to the underwriter must be approved at a meeting of the shareholders by a majority of independent shareholders. The voting must be conducted by a poll rather than a show of hands.[110] The resolution is also referred to as the ''white wash'' resolution.[111] The Panel may, in exceptional circumstances, consider waiving the requirement for a general offer, on condition that independent shareholders approve the transfer of existing shares from one shareholder to another. [112]

The practical effect of the mandatory offer has been summed up as follows: it discourages a shareholding of interests in shares carrying more than 29,99 percent of a company; it discourages a voluntary bidder from acquiring shares on the market if it wishes to make a voluntary offer subject to various types of conditions; and, it encourages persons who may be "acting in concert" and who are close to or above 30 percent to consult the UK Panel. Due to these reasons, mandatory offer bids are not frequent.[113]

In its annual report for the year 1991, the UK Panel summed up the reason for rule 9 of the City Code in respect of the mandatory offer rule as follows:

[108]Note 1 under Rule 9 of the UK City Code.
[109]Note 1 under Rule 9 of the UK City Code.
[110]C Pearson & N Adams "Mandatory and Voluntary Offers and their Terms" in M Button (ed) *A Practitioner's Guide to the City Code on Takeovers and Mergers* (2006/2007) 144.
[111]See Appendix 1- Whitewash Guidance Note, in the UK City Code. The importance of the waiver is notable from the extensive Guidance Note setting out what applicant must do to be entitled to the dispensation. The guidance note also provides transactions that may disqualify applicants.
[112]Note 1 under Rule 9 of the UK City Code.
[113]Pearson & Adams in Button (ed) *A Practitioner's Guide to the City Code on Takeovers and Mergers* (2006/2007) 150.

> "The philosophy underlying this Rule is that, if effective control of a company is obtained by the acquisition of shares, the principle of equality of treatment for shareholders requires that all shareholders should have the opportunity to obtain the price per share paid for control (it will usually be a premium price) and that they should have the opportunity to get out of the company if they do not like what has happened."[114]

The Hearings Committee of the UK Panel, in the matter of Principle Capital Investment Trust PLC ("PCIT")[115] concerned allegations that certain parties 'acting in concert' acquired the shares of PCIT and that the acquisition triggered the mandatory offer rule. Therefore, it was argued that the parties must make a mandatory offer to the remaining shareholders of PCIT. The Hearings Committee indicated that:

> "The purpose of the mandatory bid requirement is two-fold:
> to provide that, where a person obtains control of a company, he must provide the opportunity of an exit to all other shareholders in the company, since they may not wish to remain in the company now that control of the company effectively rests in the hands of a single (or different) person or a group of persons acting in concert; and on the basis that the new controller may have paid a premium price to obtain control of the company, to ensure that all shareholders in the company are granted the opportunity of an exit at the same premium price as that which may have been paid to acquire control."[116]

The UK Takeover Appeal Board upheld the decision of the Hearings Committee above in a ruling dated 13 July 2010.[117] The mandatory offer rule in the UK has been amended on several occasions in order to keep up with developments in the corporate finance industry, as practitioners become more innovative in

[114]The Takeover Panel. Annual Report 1991. Available on http://www.thetakeoverpanel.org.uk (Accessed 20-12-2013).
[115]See Takeover Appeal Board "Principle Capital Investment Trust PLC- Decision of the Appeal Board" (2010) 14 Available on http://www.the takeoverappealboard.org.uk (Accessed 20-12-2013).
[116]See Takeover Appeal Board "Principle Capital Investment Trust PLC- Decision of the Appeal Board" (2010). 14. Available on www.the takeoverappealboard.org.uk (Accessed 20-12-2013).
[117]See Takeover Appeal Board. "Principle Capital Investment Trust PLC- Decision of the Appeal Board" (2010) 14.

developing complex financial instruments and changing market conditions.[118] In particular, amendments were necessary to ensure that the mandatory offer rule kept up with newly developed financial products, such as, derivative instruments, including options.[119] The current mandatory offer rule in the City Code[120] has been amended comprehensively with the implementation of the Takeover Directive. The mandatory offer rule in rule 9 of the City Code is more stringent than in the Takeover Directive.[121] What is notable about the mandatory offer rule in the City Code is that it has not been drafted like typical regulations in South Africa. It is also applied in a flexible manner rather than according to the letter of the law.[122] A number of rules have detailed explanatory notes. These notes serve as guidelines on how the City Code should be interpreted and applied. In addition, the rules avoid the use of legalese. For instance, one finds expressions such as "the rule will not normally be …"[123] It is suggested that the style used is more suitable for self-regulatory regimes, from which the rules originates.

As the mandatory offer rule in the UK is now based on statute due to the requirements of the Takeover Directive,[124] it is important to briefly set out the principle underlying the mandatory offer rule. The Takeover Directive provides the following:

> "Article 3
> General Principles
>
> 1. For the purpose of implementing this Directive, Member States shall ensure that the following principles are complied with:

[118]The UK City Code was amended numerous times since it was a loose-leaf edition starting in 1985. See second page of 12 ed of the UK City Code (2016).
[119]See Practice Statement No 26 issued by the UK Panel to deal with Shareholder Activism dated 9 September 2009 and also Practice Statement 29 dealing with payment of inducement fees updated during 2015. Available on www.thetakeoverpanel.org.uk/up-content. (Accessed 20 -12 -2017).
[120]UK City Code (2016) The City Code was also extensively amended to bring it in line with the European Union Takeover Directive of 2004.
[121]Davies & Worthington *Gower Principles of Modern Company Law* 962.
[122]See Introduction to the UK City Code and the notes thereunder.
[123]See among others: rules 6.1, 6.2, and 8.3 of the UK City Code.
[124]Article 3 General Principle 1 of the Takeover Directive 2004.

(a) all holders of the securities of an offeree company of the same class must be afforded equivalent treatment; moreover, if a person acquires control of a company, the other holders of securities must be protected;"

The contents of the Directive were modeled almost entirely on the provisions of the City Code.[125] The general principle 1 in article 3 of the Takeover Directive is taken verbatim from City Code.[126] The wording in article 3, general principle 1 of the Takeover Directive was in the City Code even before the Takeover Directive became effective.[127] This principle provides the main rationale for enforcing the mandatory offer in various EU countries.

3 3 An evaluation of the reasons for and against application of the mandatory offer rule in the United Kingdom

The reasons for and against the mandatory offer rule, as indicated in the research, appear to be closely related, and in some instances, are similar but with a different emphasis. The rationale for application of the mandatory offer rule is to ensure that shareholders are not unduly coerced into accepting offers due to distorted information, and to protect minority shareholders from abuse.[128] It is asserted that there is a third rationale for applying the mandatory offer rule: to equalise the position between shareholders who are close to the market and those outside the market.[129] It appears that an assumption is made that institutional shareholders are close to the market while minority shareholders are not.

Presumably, institutional shareholders are closer to the market by virtue of access to research capacity while minority are outside the market due to their limited research capacity. The third rationale also supports a need to level the playing field between the well-resourced and well-informed shareholders, such

[125]Johnson (2007) Cambridge Law Journal 448.
[126]Gullifer & Payne *Corporate Finance Law Principles and Policy* 606. See General Principle 1 in the UK City Code.
[127]Gullifer & Payne *Corporate Finance Law Principles and Policy* 606.
[128]606.
[129]606.

as, institutional shareholders, and the minority shareholders, who are often uninformed. The requirement to make a mandatory offer to all shareholders meets the desire to treat shareholders equally.[130] The first two reasons for regulation of mandatory offers are in line with the general principle 1 of the City Code and the Takeover Directive dealing with the protection of shareholders and equality of treatment of shareholders.[131]

Gullifer and Payne,[132] expand the first and second rationales for the mandatory offer rule, dividing the rationale into two main categories, namely the 'undistorted choice' and the 'protection of minority shareholders'.[133] Choice distortion refers to the possibility that shareholders may be forced to accept an offer although it is not necessarily acceptable, simply because of the pressure tactics adopted by the bidder.[134] For instance, this may occur where a bidder announces an offer that will be available for a short period and limited to a set number of shareholders who accept it within the stipulated time. Such an action may distort the choice of shareholders who may accept the offer out of fear of being left in the lurch by the new controlling shareholder. In such an instance, shareholders may not exercise their free will and may not have sufficient time to consider the merits or demerits of the offer. The requirement of equality of treatment will prevent such actions by bidders since shareholders will then have to be treated equally.

It is asserted that by treating shareholders equally, there could be no distortion of shareholders' choices. The danger of 'divide and rule', where only a minimum number of shareholders get preferential treatment or special deals to entice them to accept the offer, which will ensure that the bidder gets control of the company, is prevented.[135] Therefore, it is contended that the mandatory offer

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[130]606

[131]See Takeover Directive, Article 3 General Principle 1, and also the UK City Code General Principle Number I.

[132]Gullifer & Payne *Corporate Finance Law Principles and Policy* 606-616.

[133]606-616.

[134]606.

[135]The UK City Code General Principle 1.

rule plays a crucial role in avoiding distortion of shareholders' choices.[136] The success of the rule is also bolstered by the requirement to provide sufficient information and allow enough time during the course of the mandatory offer.[137]

The second role that the mandatory offer rule plays is to protect minority shareholders in two ways: firstly, the mandatory offer rule prevents the oppression of minority shareholders,[138] and secondly, it gives minority shareholders the right to exit the company and sell their shares.[139] The reason why the mandatory offer rule is required as an additional measure in a bid, is that there is a danger that once a controlling shareholder has acquired control, it may engage in oppressive conduct to the prejudice of minority shareholders.[140] Prejudice can occur in various forms, such as, a change in the company's business strategy, withholding or even changing a company's dividend policy, and sale of company assets.[141] For this reason, shareholders must have an opportunity to exit from the company if they wish to do so. Once the bidder has made an offer to the shareholders, they are given the opportunity to sell and avoid any subsequent oppressive conduct by the new controlling shareholder. The position of minority shareholders is dependent on the identity of the new controlling shareholder, regardless of whether the new controlling shareholder will actually oppress the minority shareholders, or not.[142] The concern is rather the new direction that the company may take. The new business strategy undertaken by the new controllers may, for example, be less successful or not appealing to the existing minority shareholders.[143]

Other assertions in favour of the mandatory offer are that: the mandatory offer rule is aimed at preventing the new controlling shareholders from buying out minority shareholders at a low price, while the premium is paid to the controlling

[136]Gullifer & Payne *Corporate Finance Law Principles and Policy* 610.
[137]See the UK City Code General Principle 2.
[138]Gullifer & Payne *Corporate Finance Law Principles and Policy* 612.
[139]615.
[140]612.
[141]613.
[142]614.
[143]614.

shareholder;[144] and the mandatory offer rule serves to protect minority shareholders in that they avoid inefficient change of control in companies.[145]

The requirements of the mandatory offer rule that the new controlling shareholders should pay the same price paid to the current controlling shareholders to all minority shareholders, is controversial.[146] Objections existed even when the rule was introduced.[147] Those who are against it contend as follows: The mandatory offer requirement may be difficult to enforce, particularly during a financial downturn.[148] There is a well-accepted principle that the value of the majority shares has an inherent premium.[149] According to the mandatory offer rule, the majority shareholder cannot enjoy the value inherent in the premium attached to the controlling shares, because the premium must be shared equally among all shareholders. It has been stated that the application of the principles of equality of treatment of shareholders during takeovers are in contrast with the general UK company law, which requires that shareholders be treated fairly and not necessarily equally.[150]

The idea of treating shareholders equally seems to go against the well-accepted view that controlling shares are worth more than non-controlling shares.[151] In light thereof, it could be asked why the mandatory offer rule should require that all shareholders must be treated equally when a controlling stake is acquired.[152] Valuation experts argue that if a controlling stake commands a premium, then a minority stake should reflect a discount, taking into account its inability to control.[153] The payment of the premium in the UK is not particularly significant considering the fact that shareholding of companies in the UK is

[144] Sealy & Worthington *Sealy's Cases and Materials in Company Law* 717.
[145] See Nenova (2006) *World Bank Policy Research Paper* 4029.
[146] Gullifer & Payne *Corporate Finance Law Principles and Policy* 615.
[147] See Prentice (1972) *McGill LJ* 393.
[148] Palmer & Schmitthoff *Palmer's Company Law* 1194.
[149] Gullifer & Payne *Corporate Finance Law Principles and Policy* 614.
[150] 606.
[151] 606.
[152] 606.
[153] RA Booth "Minority Discounts and Control Premiums in Appraisal Proceedings" (2001) SSRN Available at http//ssrn.com/abstract=285649. (Accessed 20-5-2013).

widespread.[154] However, in countries where shareholdings are concentrated, this aspect of the rule is difficult to justify.[155] Discussions on valuations and how discounts or premia are applied during the valuation of a company that is the subject to a takeover or a merger is beyond the scope of this dissertation.

Another argument against the mandatory offer is that the rule deters acquirers from attempting to acquire control of a poorly-performing company. This removes the advantages of a free market for the transfer of corporate control. Because acquirers will have to ensure that they have enough cash to buy out all shareholders of the offeree company.[156] This requirement may actually prevent the bidder from paying a premium, as previously mentioned, as such a payment is likely to increase the cost of the takeover.[157] The mandatory offer rule may be a disincentive to make bids due to increasing costs of bids.[158] The mandatory offer requirement may, in fact, work against the promotion of takeovers since it increases the cost of undertaking such a takeover.[159]

It is generally asserted that takeovers improve corporate governance. However, the mandatory offer rule seems to be working against corporate governance as it discourages takeovers.[160] The additional cost required to buy the entire issued capital rather than only the controller means there will be fewer changes of corporate control. This undermines the credibility of the threat of a hostile takeover as a mechanism for forcing directors to promote shareholder value.[161]

The primary aim of the drafters of the City Code was not to promote standards of corporate governance in general but to maintain investor confidence.[162] The

[154]Gullifer & Payne *Corporate Finance Law Principles and Policy* 615.
[155]615.
[156]Prentice (1972) *McGill LJ* 393.
[157]Gullifer & Payne *Corporate Finance Law Principles and Policy* 615; see also Davies & *Worthington Gower Principles of Modern Company Law* 968-969 has similar views.
[158]See Davies & Worthington *Gower Principles of Modern Company Law* 969.
[159]McCahery & Vermeulen (2010) *Tilburg University, Tilburg Law and Economic Center*.8. See also Baum (2006) *University of Tokyo Journal of law and Politics,* referring to the UK City Code concurs that the mandatory offer rule makes takeovers more expensive.
[160]Gullifer & Payne *Corporate Finance Law Principles and Policy* 615.
[161]Johnston (2007) Cambridge Law Journal 451.
[162]451.

'right to exit' to ensure the protection of minority shareholders under the mandatory offer rules, are not properly justified.[163] Even without a change of control, the existing controlling shareholders may still develop a new strategy to the detriment of minority shareholders, but in such a case, shareholders will have no right to exit.[164] Company operations may also change due to changes of control resulting in increased shareholder value.[165] It may be argued that there may well be benefits and disadvantages during a change of control and that these outcomes should not be restricted by the mandatory offer rule.[166]

3 4 Concluding remarks

Based on the discussion above, it appears that the concerns about abusive conduct and potential prejudice to remaining shareholders by new controlling shareholders led to the introduction of the mandatory offer rule. In addition, concerns expressed by financial markets regulators, directors and market participants about fraud and a lack of disclosure, played a pivotal role in the introduction of the mandatory offer rule. [167] The rule has since been adapted over a period of time based on the general principles relating to the protection of investors. One of the aims of the rule is to ensure equal treatment of all shareholders – the requirements for equality consist of the opportunity to sell, and to sell at the same price as the exiting controlling shareholders. However, the sharing of the premium makes it impossible to sell at a premium since the purchaser knows that it will have to make the same offer to all other shareholders.[168]

In the UK, regulation of takeovers and mergers, including mandatory offers, is done based on the general principles set out in the City Code. The independent Panel, in collaboration with the Financial Services Authority, plays a major role

[163]Gullifer & Payne *Corporate Finance Law Principles and Policy* 615.
[164]615.
[165]615.
[166]615.
[167]Rosenzweig (2007) *Duke Journal of Comparative & International Law.* See also Luiz *An Evaluation of the South African Securities Regulation Code on Takeovers and Mergers.*
[168]Davies & Worthington *Gower Principles of Modern Company Law* 969.

in the success of enforcing the mandatory offer rule. There is a close relationship between the UK Panel and the parties being regulated as the Panel members are made up of industry members.[169] Therefore, the stakeholders who are regulated by the UK Panel are well represented in the decision-making committees of the Panel, both when the rules are made and when they are enforced.[170] The relationship between the UK Panel and the financial community lends credibility to the rules of the City Code and also builds trust between the financial services market participants.[171] Consequently, participants are more likely to abide and comply with the rules as they have a role to play in their enforcement and because they believe that these rules are in their interests. It is arguable that the success of this model in the UK does not necessarily support its replication elsewhere.

It is asserted that the pillars of the UK model of regulation particularly favours minority shareholders in countries that have widespread ownership structures. Few mandatory offers are actually made in the UK.[172] Due to the fact that the mandatory offer rule has been developed to provide for the circumstances that existed in the UK, it may not be appropriate for every country without modification.[173]

It appears that the drafters of the Takeover Directive considered this view. The Takeover Directive allows countries to provide derogations from the mandatory offer rule and also opt out of certain provisions. It has been indicated that in the context of the mandatory offer rule "the exception is the rule."[174] To accommodate company laws and the types of companies in different countries, the EU has accepted breakthrough rules that may be applicable where a company has defences in its charter that prevents a takeover. The main effect

[169]See UK City Code.
[170]The UK Panel operates through various committees. See the discussions under paragraph 3 2 2 above.
[171]Rosenzweig (2007) *Duke Journal of Comparative and International Law* 224.
[172]Davies & Worthington *Gower Principles of Modern Company Law* 963 and also in Wiblin "Mandatory takeover offer too high a price for the economy to pay" (2004) *Journal for Juridical Science* 3.
[173]Bockli et al (2014) *University of Cambridge Faculty of Law Legal Studies*. Paper No.5/2014.7.
[174]7.

of the breakthrough rule is to facilitate a takeover bid of companies whose charters limit the number of shares shareholders may acquire. Once a particular threshold is acquired, the break-through rules would override any limitations of the number of shares set by the company charter. In their words, control could be 'broken through."[175] This is in recognition that different countries have different needs that should be accommodated. It is also in recognition that some company structures may likely impede takeovers and mergers. Under the Takeover Directive, the mandatory offer rule is applied, but is adapted to suit different economic conditions.

The mandatory offer rule forms part of strategies implemented by UK financial participants in an attempt to protect investors. A question may be asked whether the mandatory offer rule should be applied in other countries. The rationales for the application of mandatory offers in the UK, and the institutions and the rules created to enforce rules have clearly been designed specifically for UK financial markets. The rules may not be appropriate or as effective in other countries.[176] The mandatory offer rule may not be suitable for application in other countries for a number of reasons, including the differences between the UK's financial markets and economic conditions, and those of other countries.

[175]McCahery & Vermeulen (2010) *Tilburg University, Tilburg Law and Economic Center* 10.
[176]See Bockli et al. 2014 *University of Cambridge Faculty of Law Legal Studies*. Paper No.5/2014. The discussions in the paper indicate some of the challenges of applying the mandatory offer rule across the EU.

Chapter 4: An overview of the regulation of takeovers and mergers in Australia

"The Australian experience seems to indicate an initial preparedness to adapt the received law in response to local circumstances."[1]

4 1 Introduction

In this chapter, the dissertation deals with an overview of the regulation of takeovers and mergers in terms of Australian takeover law. The previous chapter dealt with the mandatory offer as applied in the UK. Even though Australian company law,[2] like South African company law,[3] originated from the UK, their takeover and merger regime is different in respect of their provisions and the bodies regulating takeovers and mergers. There is a notable distinction - particularly the absence of a mandatory offer rule as applied in the UK. It is important to understand the rationale for Australian authorities deviating from the UK takeover and mergers rules, particularly, the mandatory offer rule.

4 2 The development of takeover and merger provisions in Australia

4 2 1 The developments leading to takeovers and mergers provisions in Australia

English company law was introduced into Australia over a period of time. This then developed into modern companies based on Australian legislation.[4] Australian company law is often seen as a mere "copy" of English company law.[5] However, there are distinguishing features that defy the assertion that

[1] P Lipton "History of Company Law in Colonial Australia: Economic Development and Legal Evolution" (2007) 31 *Melbourne University Law Review.* 830.
[2] 805.
[3] HS Cilliers, ML Benade, JJ Henning, JJ Du Plessis & PA Delport *Corporate Law* (1992) 16.
[4] Lipton (2007) *Melbourne University Law Review* 807.
[5] 806.

Australian law is "a wholesale imitation of the law of England".[6] Australian company law had already laid foundations of company law prior to the promulgation of limited liability companies' legislation based on UK company law.[7] Some of the countries, which adopted the English company law at an early stage quickly, developed thriving economies.[8] These thriving new economies encouraged inward investment, and they quickly developed successful, well-managed companies and other institutions. These developments also led to innovations and increased entrepreneurship.[9] Based on these developments, it is suggested that there is an inter-relationship between economic development, and the evolution of company law in various countries.[10] Companies and other institutions assisted in developing a healthy and well-managed economy.[11] The new institutions also created confidence in the economies of the thriving states, as investors felt protected.

Based on the Australian example, it could be argued that a strong and appropriate regulatory culture encourages rapid economic development. Lipton asserts that those countries that made rapid economic progress often also had well-developed legal systems. Well-developed and well-managed public institutions were catalysts for growth in the economies of those countries. It is suggested that the countries that had English law transplanted at an early stage also saw their economies developing rapidly due to increased investments.[12] However, a question was raised as to whether the adoption of the English law by Australian companies was suitable for local conditions.[13] It appears that the Australian authorities acknowledged that this may not necessarily have been appropriate and hence designed a different takeover regime that is discussed in the following section. From the literature reviewed, it appears that development of takeover law in Australia and Australian company law in

[6]Lipton (2007) *Melbourne University Law Review* 806.
[7]822.
[8]805.
[9]828.
[10]822.
[11]822
[12]812.
[13]806.

general has been slow and tortuous. For a considerable time, regulation of companies was done separately by the various states. Although it was accepted that there was a need for unified national securities and companies' regulations, this did not happen for a considerable time.[14]

It is generally accepted that takeovers and mergers allow companies to diversify risk and better grow their revenue base due to their bigger size. It is also acknowledged that a takeover or merger allows for the replacement of non-effective managers. However, these justifications are not universally accepted. Some researchers hold that takeovers are undertaken for the benefit of institutional investors and that managers often undertake mergers or takeovers in pursuit of short-term gains.[15]

4 2 2 Reasons for the development of takeover and merger provisions in Australia

The bust of the 1890's followed the economic boom of the 1880's. The frauds and malpractice in companies that often took place led to numerous changes to the Australian company law.[16] This was similar to the situation in the UK, where frauds led to an overhaul of the then existing UK company law and resulted in the introduction of the City Code.[17] By means of these reforms, the modern Australian company law was shaped. As more and more investors flocked into Australia, authorities saw a need to develop effective provisions for investor protection. This led to the introduction of numerous provisions relating to compulsory disclosures. Presumably, it was considered that more disclosures made to investors by companies would assist investors in making informed decisions about their investments in those companies. Regulation of

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[14]B Mees & I Ramsay *Research Report Corporate Regulators in Australia* (1961-2000): From Companies' Registrars to the Australian Securities and Investments Commission (2008) Available at: http (Accessed on 20-10-2013).
[15]I Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* (2010) .3.
[16]Lipton (2007) *Melbourne University Law Review* 822.
[17]See the discussions in Chapter 3 paragraph 3 2.

takeovers in Australia have since the 1960s "vacillated between attempts at rigid control and a practically *laissez faire* approach."[18]

The development of current takeover laws in Australia may be attributed to the successive corporate scandals of the late 1980s and the early 21st century.[19] These scandals led to the introduction of corporate regulation of takeovers by the federal authorities and the formation of the Australian Securities and Investments Commission to oversee the regulation of takeovers and mergers. Concerns about more corporate scandals led to the establishment of numerous committees whose mandate was to develop laws and procedures that were aimed at protecting investors. The various committees had varying degrees of success. It appears that some of the states resisted what they saw as 'interference' by the federal government in undermining their power to register companies. It is also suggested that this resistance from the states led to slow reforms of company law.[20]

The Eggleston Committee,[21] named after Sir Richard Eggleston, the convener, was one of the many committees that contributed to important developments in the regulation of takeovers and mergers in Australia. The Committee led the discussions on the introduction of new takeover and merger provisions, and introduced principles that were focused on the avoidance of mistreatment of shareholders.[22] The principles are considered to be the foundation of Australia's takeover legislation. They concentrated on four requirements, namely (1) that the identity of the bidder be known; (2) reasonable time be allowed for shareholders to consider the offer; (3) the necessary information be

[18]P Brown & R da Silva Rosa "Australia's Corporate Law Reform and the Market for Corporate Control" (1998) 5: 2 *Agenda* 179-188.
[19]A Dignam "Lamenting Reform? The Changing Nature of Common Law" (2007) 25 *Corporate Governance Regulation' Company and Securities Law Journal* 283-299. 2.Available at: http//ssrn. com/abstract=1839447. (Accessed 20- 5- 2017).
[20]Lipton (2007) *Melbourne University Law Review* 826.
[21]J Lessing "Corporate takeovers: Law Reform and Theory- Is The minority shareholders being disadvantaged? (1997) 9 BLR.6. The committee sat during 1969 and its principles became to be known as the Eggleston Principles.
[22]M Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in I Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* (2010) 39.

provided to shareholders to make an informed decision; and (4) an equal opportunity be granted for shareholders to participate in the offer.[23] The Eggleston Principles are primarily concerned with distributive justice.[24] It is suggested that the conflicts between demands for equity and motives for making a profit need to be given greater consideration by means of a clear policy.[25] A number of researchers do not seem to share the view that the Eggleston Principles benefit shareholders. In their view, these principles are principal stumbling blocks to a policy overhaul that would favour market activity.[26]

The same concerns that shareholders may be treated unfairly during takeovers and mergers no doubt also apply in Australia. A view has been expressed that rules to regulate takeovers and mergers are intended to benefit target shareholders, as during a tender offer bid, target shareholders often do not benefit as much as they should.[27] This situation may leave many target shareholders with no real choice, and prevents competing bids by rival bidders that would have benefited all shareholders. It is suggested that this is due to the fact that, in takeovers or mergers, most shareholders have very little power and, therefore, limited choice. It is asserted that the growing dissatisfaction with these features of the marketplace for corporate control led to the introduction of similar regulatory measures in the UK. It is further indicated that some of the strategies which pressured target shareholders include coercing target shareholders into accepting the offer, holding target shareholders bound to the offer and ensuring that bidders retain maximum leeway with respect to the offer.[28] Bidders are able to coerce target shareholders into acceptance by use

[23]Guidance note GN 1 (guidance note 1) and also RB Thompson "Takeover Regulation After the "Convergence" of Corporate Law" (2002) *Vanderbilt University Law School Law & Economics* 6 Available at http://ssrn.com/abstarct id= 362880 (Accessed 15-2-2014).
[24]Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 39.
[25]B Sheehy "Australia's Eggleston principles in takeover law: Social and economic sense?" (2004) *Australian Journal of Corporate Law* 6.
[26]Brown & da Silva Rosa (1998) *Agenda* 179-188.
[27]R Sappideen "Takeover Bids and Target Shareholder Protection: The Regulatory Framework in the United Kingdom, United States and Australia" (1986) 8 *Journal of Comparative Business and Capital Market Law* 281-317, 281.
[28]Sappideen (1986) *Journal of Comparative Business and Capital Market Law* 281.

of the partial bid together with acceptances based on a first-come, first-served basis. [29] This means that only a limited number of the shares are bought. Furthermore, according to the first-come first-serve offers, the sellers' shares are accepted in the order by which they are tendered into the offer. This tactic results in the creation of a prisoner's dilemma for target shareholders. Those who do not tender into the offer while other shareholders do so will not have the opportunity to accept the offer once the offer is closed. Shareholders may fear being left in a company that had substantial change of shareholding. On the other hand, they may not have the full details of the offer due to the time limit and tactic adopted by the bidder to ensure that the shareholders have little time to respond to the offer. Hence the prisoner's dilemma. The bidders could also attempt to strengthen their position by making their offers subject to a number of conditions that further add uncertainties to the bid. This also weakens the position of target shareholders.[30]

The main principles for regulating takeovers and mergers are now set out in terms of section 602 of the Corporations Act 2001. In short, this section requires that:

> "(a) changes of control in respect of certain companies including listed companies, or an unlisted company with more than 50 shareholders takes place in an efficient, competitive and informed market;
>
> (b) shareholders or holders of relevant interests and the directors of the company or body or the responsible entity for the transactions know the identity of any person who proposes to acquire a substantial interest in the company, body or scheme and have a reasonable time to consider the proposal;
>
> (c) the shareholders and such persons or bodies, or entities, in (b) above, are given enough information to enable them to assess the merits of the proposal; and

[29] 281.

[30] Sappideen (1986) *Journal of Comparative Business and Capital Market Law* 282.

(d) that an appropriate procedure is followed as a preliminary action to a Compulsory acquisition of voting shares or interests or any other kind of securities."[31]

The first three requirements form the core of the Eggleston Principles. The last principle was introduced by section 602 of the Corporations Act 2001.These principles form the foundation of the Australian merger and takeover provisions in their modern form. Section 602 of the Corporations Act 2001 is "remarkably faithful to the Eggleston Principles".[32] Section 602(d) of the Corporations Act 2001 was added by the legislature to ensure protection of minority shareholders, as they are able to sell their shares to the acquirer where the acquirer has acquired 90 percent of the relevant voting securities. In the same way that the acquirer is forced to buy out the minority shareholders, subject to safeguards put in place by the courts, this section forces a major shareholder to acquire the shares of minority shareholders. [33]

While the Eggleston Principles and section 602 of the Corporations Act 2001 set out the basic principles for regulating takeovers and mergers, the fundamental approach in Australian takeover law is a general takeover prohibition contained in section 606 of the Corporations Act 2001. The basic approach is that an acquisition of 20 percent of the voting rights in a company is not allowed, unless certain principles have been complied with. Unless there is compliance with the takeover and merger provisions, no such acquisitions must be made.[34] The Australian takeover regime is a uniquely restrictive hybrid.[35] It has elements of the UK City Code and of the US takeover rules. Hence, it is pointed out that the Australian model of takeover regulations did

[31]Australian Corporations Act 2001.
[32]Sheehy (2004) *Australian Journal of Corporate Law* 2.
[33]ASIC Regulatory Guide 10 Compulsory acquisitions and buyouts (2013) Available at:http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/rg10-published-21-June-2013.pdf/$file/rg10-published-21-June-2013.pdf> (Accessed 20-2-2014).
[34] King & Wood Mallesons "A guide to takeovers in Australia" (2012) Available at: http://www.mallesons.com/Documents/A_guide_to_takeovers_in_Australia.pdf> (Accessed 20-2-2014).
[35]E Hutson "Australia's takeover rules: how good are they?" (2002) *Corporate Regulation, Jassa Issue* 4 *Summer* 33.

not “borrow wholesale” from the UK City Code.[36] Most important for this dissertation is that the mandatory offer rule that exists in the UK was not adopted by Australia.[37]

The Corporate Law Economic Reform Program Bill 2003, commonly referred to as the CLERP, introduced a new way of regulating mergers and takeovers in Australia. Disclosures form an important part of the regulatory regime in takeovers in terms of these reforms. It is generally accepted that disclosures about takeovers assist shareholders to make informed decisions about the value of their company shares. Continuous disclosures enable investors to protect themselves and plan accordingly. The CLERP memorandum indicates that the existence and enforcement of Australia’s continuous disclosure laws are fundamental to the efficient operation and protection of its financial and securities markets.[38] During the CLERP reforms, Australia considered introducing a mandatory offer and comments on the matter were requested.[39] However, the legislator finally decided against it. A mandatory rule did not find its way into the Corporations Act 2001. The idea was abandoned as it was not supported by the non-government parties at the time.[40] One of the concerns was that it had possible adverse impact on a competitive market for corporate control as it reduced the opportunity for auctions for control.[41]

However, the absence of a mandatory offer bid in Australia does not mean that minority shareholders are not protected, although it may at first sight, appear so. The equal treatment rules in Australia are more rigid than those of the UK City Code.[42] While in the UK, a mandatory offer is applicable once the offeror moves over 30 percent threshold, “The offeror for an Australian company

[36]See Dignam (2007) *Company and Securities Law Journal* 283-299.
[37]See above 283-299.
[38]Australian Government *Corporate Law Economic Reform Program Bill* (2003) Available at: http://www.takeovers.gov.au/content/Resources/acts_bills_ems.aspx. (Accessed 20-8-2013).
[39]Emma Armson ‘Evolution of Australian Takeover Legislation’ (2012) Vol 39, No 3 *Monash University Law Review* 682.
[40]Armson (2012) *Monash University Law Review* 683 at note 252.
[41]Armson (2012) *Monash University Law Review* 682.
[42]J Mannolini ‘*Convergence or Divergence: Is there a Role for the Eggleston Principles in a Global M&A Environment* ‘(2002) Vol 24:336 *Sydney Law Review* 358.

cannot acquire control of a parcel of more than 20 per cent, except *pursuant to* a general offer."[43] Therefore, a minority shareholder in Australia tends to "be empowered to a far greater extent than in the United Kingdom".[44]

The approach of regulators over the world is that regulating takeovers and mergers is important from the perspective of all stakeholders, including shareholders. Shareholders need to be protected during the course of a takeover and they need to be able to make an informed decision about whether to sell or retain their shares during a bid. These fundamental principles of regulating takeovers and mergers also form the cornerstone of regulating takeover and mergers in Australia.

4 2 3 Bodies responsible for regulating takeovers and mergers

The Australian Securities and Investments Commission (ASIC) and the Australian Takeovers Panel (Australian Panel) are the two regulating bodies responsible for takeover and merger regulation in Australia. Each of them performs a separate regulatory function in respect of takeovers and mergers. ASIC is Australia's corporate, markets and financial services regulator and ensures that Australia's financial markets are fair and transparent, and supported by confident and informed investors and consumers.[45] It has been set up under, and is administered in terms of, the Australian Securities and Investments Commission Act No 51 of 2001 (ASIC Act)[46] and carries out most of its work under the Corporations Act 2001.[47] On the other hand, the Australian Panel is an adjudicator of disputes that may occur during a takeover or a

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[43]Mannolini (2002) *Sydney Law Review* 358.
[44]Mannolini (2002) *Sydney Law Review* 358.
[45]See Australian Securities and Investments Commission Available at: http//www. asic.au.gov. (Accessed 20-2-2014).
[46]Section 8 Section 8 of the Australian Securities and Investments Act No 51 2001 provides that ASIC:
(a) is a body corporate, with perpetual succession; and
(b) has a common seal; and
(c) may acquire, hold and dispose of real and personal property; and
(d) may sue and be sued in its corporate name.
[47]See Australian Securities and Investments Commission June 2013, Regulatory Guide 9 <http// www.asic.au.gov.> (Accessed 20-2-2014)).

merger.[48] The Panel was created in terms of section 171 of the ASIC Act. It is inevitable that in their regulatory spheres, ASIC and the Australian Panel will often cross paths, even though they regulate different aspects of takeovers and mergers. It is also important that the two bodies co-operate in order to ensure maximum compliance.

The Australian takeover and merger provisions apply to companies listed on the Australian Securities Exchange, private companies that have more than 50 shareholders, corporate bodies, even if such bodies are not companies that are formed in Australia, and listed managed investment schemes**.**[49]

4 2 3 1 The Australian Securities and Investments Commission

ASIC was established by section 7 of the Australian Securities and Investments Commission Act of 1989 and has continued to exist in terms of section 261 of the Australian Securities and Investment Commission Act of 2001. ASIC has the functions and powers that are conferred on it by, or under, various Australian acts.[50] Some of those functions and powers are not relevant for the purposes of this dissertation. It also has numerous broad functions including monitoring and promoting market integrity and consumer protection in relation to the Australian financial system, and monitoring and promoting market integrity and consumer protection in relation to the payments system. It is required to undertake a number of steps in order to achieve its mandate. The steps include public awareness and educating consumers.[51] ASIC may also

[48]See The Australian Takeover Panel <www.takeoverspanel.au.gov. (Accessed 20-2-2014).
[49]Sections 602, 602A, 603 and 604 of the Australian Corporations Act No 50 of 2001.
[50]The Acts include:(a) the Insurance Act 1973; (b) the Insurance (Agents and Brokers) Act 1984; (c) the Insurance Contracts Act 1984; (d) the Superannuation (Resolution of Complaints) Act 1993; (e) the Life Insurance Act 1995;(f) the Retirement Savings Accounts Act 1997; and (g) the Superannuation Industry (Supervision) Act 1993.
[51]In accordance with the above functions, ASIC is required to undertake the following:
(a) promoting the adoption of approved industry standards and codes of practice; and
(b) promoting the protection of consumer interests; and
(c) promoting community awareness of payments system issues; and
(d) promoting sound customer-banker relationships, including through:
(i) monitoring the operation of industry standards and codes of practice; and
(ii) monitoring compliance with such standards and codes.

advise the Minister about any changes to a law or advise the Minister to make recommendations about any matter relating to its functions.

ASIC can be termed a ‘super regulator’ due to its comprehensive regulatory functions and powers.[52] In contrast, in South Africa, the functions performed by this singular body are spread across various independent regulatory bodies, such as, the Financial Sector Conduct Authority,[53] which administers various financial-services statutes, the National Credit Regulator[54] (which deals with matters relating to credit), the National Consumer Commission[55] (which resolve consumer related matters), the Companies Commission (which administers the Companies Act of 2008),[56] the Companies Tribunal[57] (which resolves certain disputes in terms of the Companies Act of 2008) and the SA Takeover Regulation Panel (SA Panel)[58] in reviewing merger and takeover documents, and The Takeover Special Committee.[59] (which resolves disputes in respect of mergers and takeovers in terms of the Companies Act of 2008).

Among its many functions, ASIC is responsible for reviewing takeover and merger documents in terms of the Corporations Act 2001. It may also investigate, monitor, prosecute and develop policies in respect of mergers and takeovers. In terms of section 655A of the Corporations Act 2001, ASIC has the power to exempt any person from any of the provisions in chapter 6 of the Corporations Act 2001. The power of ASIC to exempt is, however, subject to the provisions of section 602 of the Corporations Act 2001 – the main principles for regulating takeovers and mergers. ASIC must consider these principles before any exemption may be granted. Where the application for exemption will be against the purpose and principles set in section 602, such an exemption will not be granted.

[52]ASIC is responsible for administering a number of legislations. See note 50 above.
[53] See section 58 of the FSR Act which set the functions of the Financial Sector Conduct Authority.
[54]Section 12 of the National Credit Act No 34 of 2005.
[55]Section 85 of the Consumer Protection Act No.68 of 2008.
[56]Section 185 of the Companies Act 71 of 2008.
[57]Section 193 of the Companies Act 71 of 2008.
[58]Section 196 of the Companies Act 71 of 2008.
[59]Section 202 of the Companies Act 71 of 2008.

The role of ASIC in supervising takeovers and mergers incudes administration and monitoring how takeover bids are conducted.[60] The differences between the Australian Panel, ASIC and the SA Panel in regulating takeovers and mergers will be dealt with in chapter 6. In the Regulatory Guide 9 on takeover bids, ASIC has indicated that the functions and powers of ASIC as an overseer of takeovers and mergers, among others, include: (a) reviewing and monitoring of documentation, disclosures and conduct in relation to bids to ensure compliance with the takeover provisions; (b) providing regulatory guidance and relief that improve commercial certainty and balance the protections of the takeover provisions; and (c) in applicable cases, taking enforcement action to protect the interests of investors and promote their confident and informed participation in the takeover process and financial markets, generally.[61]

ASIC's regulatory role in undertaking surveillance of takeovers and mergers, its day-to-day administration role and its enforcement role with respect to takeovers, are supported and complemented by the role of the Australian Panel, which is the main forum for resolving disputes concerning takeover or merger transactions. ASIC also regulates schemes of arrangement undertaken in terms of the Corporations Act 2001 that are aimed at achieving a change of control of a corporation in a similar way as may be achieved by a takeover offer. ASIC's coordinated efforts in regulating mergers and takeovers is aimed at ensuring that, as far as practically possible, similar principles and protections are afforded to investors, regardless of whether control acquisition is through a scheme of arrangement or a takeover bid.[62] In regulating takeover bids including schemes of arrangements, ASIC applies the general principles set out in section 602 of the Corporations Act 2001.[63] In terms of this guideline,

[60]Australian Securities and Investments Commission, issued December 2016, Regulatory Guide 9. Available at https//www.asic.au.gov. (Accessed 19 February 2019).
[61]Regulatory Guide 9 paragraphs 9.6.
[62]See Australian Securities and Investments Commission, Regulatory Guide 60 (Regulatory Guide 60), dealing with *Schemes of arrangement* Available at: https// www. asic.au.gov. (Accessed 20-2-2014
[63]Regulatory Guide 9 and Regulatory Guide 60.

ASIC follows what it terms as “truth in takeover”.[64] Hereby, ASIC ensures that the schemes of arrangement comply with the basic principles of full disclosure, fairness and equality of treatment, among others, when it examines the documents relating to schemes, the proposed scheme and the draft explanatory statement for the scheme.[65] ASIC also reviews and makes inquiries during a takeover. Certain documents must be lodged with ASIC as part of the takeover or merger process, which may include agreements or irrevocable undertakings relating to the takeover or merger. The review process may consider the terms, conditions and structure of the takeover or merger, as well as the disclosures made in the various documents. According to the ASIC guideline, ASIC has a general power to refuse to register or receive a document submitted for lodgement that does not comply with relevant procedural requirements.[66]

During their review process, ASIC may also make additional inquiries in relation to a takeover to ensure that relevant parties are complying with their obligations. ASIC may undertake the inquiries at their own initiative or as a result of a complaint lodged by any interested party. The inquiries may be broad and include questions about the conduct of parties during a takeover or merger, and announcements or comments made in the media during the takeover process. In undertaking their reviews or inquiries, ASIC’s point of departure is the principles set out in section 602 of the Corporations Act 2001. ASIC considers whether the conduct of the parties or announcements made during a takeover has any detrimental effect or undermines the principles set out in section 602 of the Corporations Act 2001. In this way, any misleading information is addressed. Parties may then be required to issue corrective statements. Failure to reach an agreement with parties may lead to an application to the Australian Panel to declare particular conduct as an unacceptable circumstance in relation to a takeover or a merger.

[64] Regulatory Guide 9
[65] See Regulatory Guide 60
[66] See Regulatory Guide 60

When ASIC exercises its discretionary powers in terms of section 655A of the Corporations Act, one of the main considerations in granting exemption from the requirements of section 602 of chapter 6 is that such an exemption does not negatively impact on the principles set out in section 602.[67] ASIC also has the power to grant class orders, grant modifications, grant specific consent or approvals, and to make market integrity rules.[68] In terms of section 631 of the Corporations Act 2001, it is an offence if a person publicly proposes to make a takeover bid and then does not proceed to make offers under that bid within two months of the proposal. This law is in place to ensure that announced takeovers are followed through and offers are actually made. ASIC and the Australian Panel have a co-operative relationship. ASIC has standing to apply to the Australian Panel for a declaration of unacceptable circumstances in relation to the affairs of any company or listed registered managed investment scheme.

In cases where other parties apply to the Australian Panel for a declaration, ASIC must be invited to make submissions on the matter and on any orders that the Australian Panel proposes to make in terms of section 657A(4) and 657D(1) of the Corporations Act 2001. In deciding whether or not to make submissions, ASIC considers the following:
(a) whether unacceptable circumstances exist in relation to a takeover bid; (b) whether interests of parties may be affected by the relevant circumstances and such parties are not represented in the proceedings – in particular, retail or minority investors; (c) whether the issues raise matters of policy or interpretation that may have wider implications for the conduct of takeovers in general; (d) whether it has had any previous involvement or engagement with the matter or dispute at hand; and (e) whether they are in a position to provide any factual information that may assist the Australian Panel.[69] ASIC and the Australian Panel have entered into a memorandum of understanding (MOU) to enhance cooperation in their respective roles in takeovers. The MOU deals with

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[67]The section setting out the main principles underlying regulation of takeover and mergers in Australia.
[68]See Regulatory Guide 9
[69]Regulatory Guide 9.

information-sharing, consultation on policy development and regular liaison between the parties.[70]

4 2 3 2 The Australian Takeovers Panel

Regulation of takeovers and mergers in Australia was initially entrusted to the National Companies and Securities Commission and finally to the current Australian Panel.[71] Due to the concerns that it is not appropriate to vest the powers of an investigator and an adjudicator in the same body, there was a need to separate these two powers. This led to the establishment of the Australian Panel. The Australian Panel initially existed as the Corporations and Securities Panel, finally changing its name to the Australian Panel, as it is still known today.[72] Prior to the restructuring of the Australian Panel to its current form, it was regarded as ineffective. Most disputes had to be settled by the courts.[73] Ramsay,[74] for example, agrees with the assertion and indicates that the Australian Panel was not successful prior to the introduction of the changes by the Corporations Act 2001 (Australian Corporation Act). Initially the Australian Panel struggled with limited jurisdiction, with a legal framework that hindered its operations. ASIC also did not want to refer disputes on takeovers to the Australian Panel as it was supposed to do so in terms of the regulatory regime.

The Panel has been established in terms of section 171 of the ASIC Act and is given its powers under part 6.10 of the Corporations Act 2001. It carries out its functions and mandate in terms of chapter 6 of the Corporations Act 2001.[75] The Australian Panel is a peer review body and its members consist of various

[70]Australian Securities and Investments Commission June 2013, Regulatory Guide 9.
[71]Ramsay "The Takeovers Panel: A Review" in *The Takeovers Panel and the Takeovers Regulation in Australia* 34.
[72]34.
[73]N Calleja *The New Takeover Australian Panel –A Better Way?* (2002) 5.
[74]Ramsay "The Takeovers Australian Panel: A Review" in *The Takeovers Australian Panel and the Takeovers Regulation in Australia* 34.
[75]658-659.

industry practitioners.[76] The Australian Panel comprises legal and commercial experts in the area of takeovers and mergers.[77]

The Panel members are appointed by the Governor-General, on nomination by the Minister, in terms of section 172 of the ASIC Act. There must be a minimum of five members and they are nominated based on their knowledge or experience.[78] On 28 June 2013, the Australian Panel had 48 members.[79] Australian Panel members perform their functions on a part-time basis and the executive of the Australian Panel undertakes the day-to-day regulatory guidance. The executive of the Australian Panel consists of at least four persons, namely, the director, counsel and two support staff members, and up to two secondees who usually come from law firms.[80] The sitting members of the Australian Panel (as members who are responsible for adjudicating a dispute is known) are supported by the executive team and a president chairs the Australian Panel proceedings.[81] The executive team of the Australian Panel is not involved in the dispute resolution process of the Australian Panel, but rather play an important role in ensuring that the Australian Panel informs parties of the various procedures involved in the resolution of a takeover dispute.[82]

The executives of the Panel are the first point of contact for parties involved in any disputes. According to the notes to the rules, the executives act with the authority of the president of the Australian Panel when conducting business on behalf of the Australian Panel and when interacting with parties.[83] In order to

[76]Calleja *The New Takeover Australian Panel –A Better Way?* 1.
[77]E Armson "Working with Judicial Review: The New Operation of the Takeovers Australian Panel" (2009) 33 *Melbourne University Law Review*. 658.
[78]Australian Takeovers Panel, Panel Proceedings, Available at: http//www.takeovers.gov.au. content/DisplayDoc.aspx? doc=Panel_members.html, (Accessed on 15-2-2014).
[79]Australian Takeovers Panel Annual Report 2012-2013, Available at: http//www.takeovers.gov.au. content/resources/reports/annual_ reports.2012-2013 (Accessed on 15-2-2014).
[80]AustralianTakeoversPanelAvailableat:http://www.takeovers.gov.au/content/DisplayDoc.aspx?doc=Panel_process/the_Panel_process.htm. (Accessed 15-2-2014).
[81]Australian Takeovers Panel, Panel Proceedings, and Available at: http//www.takeovers.gov.au. content/DisplayDoc.aspx? doc=Panel_ process/ the_ Panel. html, Accessed on (15-2-2014).
[82]See Australian Takeovers Panel- About the Panel.
[83]The Australian Takeovers Panel. Procedural Rules, Note 1 to rule 10.1.

preserve procedural fairness and to make it possible to preserve independence, the parties and the president of the Australian Panel or Australian Panel members do not communicate directly.[84] The executives of the panel manage the day-to-day administrative functions of the Australian Panel. These include dealing with matters such as informing parties of the progress of their applications and advising the president of the Australian Panel or Australian Panel members about various applications and submissions, questions of law and issues of policy, when needed.[85]

Some of the specific tasks undertaken by the executive are: assisting the president to identify an Australian Panel for a matter; assisting Australian Panel members with conflict checks; conducting research for the Australian Panel; preparing draft documents for the Australian Panel such as media releases, declarations, interim and final orders and reasons for a decision; and when requested, advising and assisting the president or the Australian Panel in performing or exercising their functions or powers. According to note 3 to the rules, the executive does not make decisions on the merits of an application. They do not sift or filter information to be submitted to the Australian Panel. It is the function of the Australian Panel itself to decide on such matters.[86] Another important function of the executive is to provide market participants with the current approach on policy issues so as to provide guidance. The executive may give market participants or parties its general opinions on the Australian Panel's likely views on a particular matter or a hypothetical transaction. Such opinions, however, do not bind the Australian Panel.[87]

The primary role of the Panel is to decide whether there are unacceptable circumstances in relation to a takeover or merger, applying the principles underlying the takeover provisions set out in chapter 6 of the Corporations Act

[84] The Australian Takeovers Panel. Procedural Rules, Notes to the Procedural Rules.
[85] The Australian Takeovers Panel. Procedural Rules, Note 2 to Rule 10 of the Procedural Rules.
[86] The Australian Takeovers Panel. Procedural Rules, Note 3 to Rule 10 of the Procedural Rules.
[87] The Australian Takeovers Panel. Procedural Rules, Note 4 to Rule 10 of the Procedural Rules.

2001. In declaring 'circumstances unacceptable' in relation to takeovers or mergers the main aim of the Australian Panel is to ensure that takeover or merger transactions adhere to the policy set out in section 602, containing the main original Eggleston Principles.[88]

The Australian Panel has an internal review panel whose function is to review decisions of the hearing panel at the request of the parties or ASIC. The internal review panel will exclude those members of the Australian Panel who participated in the decision being reviewed.[89] The president of the Australian Panel must consent to the application to review the decision of the Australian Panel prior to convening the review panel.[90] In 2000, the Australian Panel gained new powers by means of the CLERP.[91] These reforms brought about major changes in how disputes in takeovers are resolved.[92] The reforms were aimed at promoting speedy, informal and uniform decision-making during the regulation of takeovers.[93] The CLERP reforms were also aimed at avoiding tactical litigation during takeover and mergers.[94] It was also hoped that by creating a specialist takeover regulatory body, the courts would be freed from being involved in takeover disputes, except in certain circumstances. Therefore, although the Australian Panel is the primary forum for regulating disputes in mergers and takeovers, the courts still have a role to play as the Australian Panel may refer questions of law to the court. The reform of the Australian Panel also ensured a more responsive body that could quickly and efficiently deal with disputes in takeovers and mergers. This also ensured that parties were not unnecessarily lumbered with high costs when resolving

[88]Section 602 also incorporate additional principles relating to efficient, competitive and informed market as well as compulsory acquisitions. See guidance note 1 at paras 30-31. and see Calleja *The New Takeover Australian Panel –A Better Way?* 3.
[89]Ramsay *"The Takeovers Panel: A Review" in The Takeovers Panel and the Takeovers Regulation in Australia* 1-38.
[90]E Armson "The Australian Takeovers Panel: Commercial Body or Quasi-Court? (2004) 58 *Melbourne University Law Review*, 2 Available at: SSRN: http://ssrn.com/abstract=887650 (Accessed 14-2-2014).
[91]E Armson "An Empirical Study of the First Five Years of the Takeovers Panel" (2005) 27 *Sydney Law Review* 665.
[92]665.
[93]665. See also Ramsay "The Takeovers Panel: A Review" in *The Takeovers Panel and the Takeovers Regulation in Australia* (2010) 34.
[94]Armson (2005) *Sydney Law Review* 665.

disputes during their transactions.[95] The Australian Panel became the main forum for regulating takeovers and this also allowed it to achieve principle-based rather than "black-letter-of-the-law regulation.[96] This approach is encouraged, as it is believed that the regulation of mergers and takeovers should be about principles and not just what the law prescribes.[97] The Australian government introduced two principal reforms, which rejuvenated the Australian Panel during 2000.[98] These are:

> "1) replacement of the black letter of the law regime with a principles based regulatory one; and
> 2) shifting the primary responsibility for dispute resolution from the courts to a tribunal comprising markets participants."[99]

It is generally known that detailed legislative requirements may create significant opportunities for tactical litigation to be used as a strategy to affect the outcome of a takeover bid or a merger. During a takeover or a merger, there are considerable incentives to pursue tactical litigation due to the conflicting interests between the bidder and the directors of the target company. The conflicts arise mainly due to the fact that the directors of the target company will lose their jobs if the takeover or merger succeeds. [100] Tactical litigation can also be pursued by legal practitioners who may be motivated by the prospect of huge success fees should they be able to defeat a takeover by another company.

The implementation of the above changes was not without difficulties. It is suggested that this is due to the fact that when a statutory regime is replaced by principle-based regulation; there is a possibility of judicial review and

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[95]Calleja *The New Takeover Australian Panel –A Better Way?* 4.
[96]Dyer & MacDonald, "Why Was the Takeover Panel Established" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* (2010) 80-96.88.
[97]B Dyer & M MacDonald "Why Was the Takeover Panel Established" in *The Takeovers Panel and Takeovers Regulation in Australia* 81.
[98]See Ramsay "The Takeovers Panel: A Review" in *The Takeovers Panel and the Takeovers Regulation in Australia* 34.
[99]S McKeon "Foreword" in Ramsay (ed) *The Takeovers Panel and the Takeovers Regulation in Australia* (2010) v-vii.
[100]Armson (2005) *Sydney Law Review* 666.

constitutional challenge.[101] This indeed happened. The Australian Panel subsequently gained constitutional recognition in the case of *Attorney General v Alinta,*[102] where the High Court upheld the constitutional validity of the Australian Panel's powers.[103] Prior to this, the provision that the Australian Panel as a primary forum for regulating disputes in takeovers and mergers was often questioned by the disputing parties and their legal representatives.[104] To reduce the use of tactical litigation, the Corporations Act 2001 significantly restricts the courts' role. The courts' involvement is restricted because the Corporations Act 2001 contains a limitation clause that restricts access to the courts during the course of the bid.[105] The Australian Panel, on its website, proclaims:

> "Under s659B of the Corporations Act, private parties to a takeover no longer have the right to commence civil litigation, or seek injunctive relief from the courts in relation to a takeover, while the takeover is current." [106]

Only governmental authorities may commence court proceedings in relation to a takeover bid during the course of a bid.[107] In line with the rule of law, the Australian Panel is subject to review by the courts – to guard against the possibility that the Australian Panel acts outside the law in exercising its powers to resolve disputes arising during a takeover bid.[108]

As indicated above, it is generally accepted by most commentators on Australian takeovers and mergers, that the Australian Takeover Panel was not effective in its first years of existence.[109] This was due to the structure of the

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[101]McKeon "Foreword" in *The Takeovers Panel and the Takeovers Regulation in Australia.* v-vii.
[102]2008 233 CLR 542. See also Armson (2009) *Melbourne University Law Review* 662.
[103]Armson (2009) *Melbourne University Law Review* 662.
[104]657-682.
[105]See section 659B of the Corporations Act 2001.
[106]The Australian Takeovers Panel Available at: http www.takeoversAustralian Panel.au.gov. (Accessed 15-2-2014).
[107]Armson (2009) *Melbourne University Law Review* 661.
[108]661.
[109]See Calleja *The New Takeover Panel –A Better Way?* 4; Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 39-79; and also, Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1-38. 34.

Australian Panel and because it could only deal with matters which had been referred to it by ASIC for dispute resolution. During the first few years of the Australian Panel's existence, ASIC referred few matters to it. Another problem was the fact that parties to a dispute could not directly approach the Australian Panel for dispute resolution, nor could complaints in respect of a takeover or a merger be lodged directly with the Australian Panel. The Australian Panel could also not resolve disputes *mero motu* but had to be reactive and wait for a referral from ASIC. It appears that the amendments introduced by CLERP improved the situation for the Australian Panel. The Australian Panel can now directly take matters for dispute resolution without any referral from ASIC. In terms of section 657C (2) of the Corporations Act 2001, any person may now request the Australian Panel to resolve any dispute in respect of a takeover or a merger. This includes the bidder, the target company, ASIC or any person whose interests may be affected by the takeover or the merger.

4 2 4 The role of the Australian Takeover Panel in takeovers and mergers

One of the most important powers of the Australian Panel is to make declarations regarding 'unacceptable circumstances' pertaining to a takeover or merger.[110] The power to declare circumstances unacceptable is created in terms section 657A of the Corporations Act 2001. The section provides that:

> **"**(1) The Australian Panel may declare circumstances in relation to the affairs of a company to be unacceptable circumstances. Without limiting this, the Australian Panel may declare circumstances to be unacceptable circumstances whether or not the circumstances constitute a contravention of a provision of this Act.
> (2) The Australian Panel may only declare circumstances to be unacceptable circumstances if it appears to the Australian Panel that the circumstances:
>> (a) are unacceptable having regard to the effect that the Australian Panel is satisfied the circumstances have had, are having, will have or are likely to have on:

[110]Ramsay "The Takeovers Panel: A Review" in *The Takeovers Panel and the Takeovers Regulation in Australia* (2010) 1-38.

(i) the control, or potential control, of the company or another company; or

(ii) the acquisition, or proposed acquisition, by a person of a substantial interest in the company or another company; or

(b) are otherwise unacceptable (whether in relation to the effect that the Australian Panel is satisfied the circumstances have had, are having, will have or are likely to have in relation to the company or another company or in relation to securities of the company or another company) having regard to the purposes of this Chapter set out in section 602; or

(c) are unacceptable because they:

(i) constituted, constitute, will constitute or are likely to constitute a contravention of a provision of this Chapter or of Chapter 6A,6B or 6C; or

(ii) gave or give rise to, or will or are likely to give rise to, a contravention of a provision of this Chapter or of Chapter 6A, 6B or 6C.

The Australian Panel may only make a declaration under this subsection, or only decline to make a declaration under this subsection, if it considers that doing so is not against the public interest after taking into account any policy considerations that the Australian Panel considers relevant."[111]

The power to declare that circumstances are unacceptable in respect of a merger or takeover is so important that the Australian Panel has issued Guidance Note 1[112] to its stakeholders, including companies and their advisers. The guidance note is intended to assist companies and the advisers, relating to conduct, practices or terms and conditions during a takeover or a merger that are regarded as inappropriate.

The circumstances under which the Australian Panel may declare unacceptable circumstances are very wide. It is notable that circumstances may be unacceptable circumstances whether or not they contravene the

[111] Corporations Act 2001, section 657A.
[112] Guidance note 1 provides examples of unacceptable circumstances.

Corporations Act 2001.[113] The guidance note issued by the Australian Panel describes a wide range of circumstances that can be declared unacceptable. The guidance note states that this is necessary to allow the Australian Panel to fulfill its role, as envisaged by the Corporations Act 2001, as the main forum for resolving disputes about a takeover bid. Applications for a declaration can only be made within two months after the alleged circumstances have occurred or such longer period that the Panel may allow.[114] The powers of the Australian Panel to declare unacceptable circumstances are subject to the overarching requirement that any declaration of unacceptable circumstances made by the Australian Panel must not unfairly prejudice any person.[115]

There is no definition in the Australian Corporations Act 2001 of what an unacceptable circumstance in respect of a merger or takeover is.[116] Although, at first sight, this power to declare such a circumstance may seem limited, it is in fact very wide.[117] It could be argued that the definition has been left out on purpose to avoid limiting the powers of the Australian Panel. An overview of the decisions taken by the Australian Panel suggests that most applications considered by the Australian Panel are to declare circumstances in respect of a takeover or merger unacceptable. In addition, the Australian Panel may make other decisions where it considers that taking into account the circumstances of a transaction, and its effect on the control or the acquisition of a substantial interest in a company may be unacceptable.[118] To protect the rights of other persons, before making the order, the Australian Panel must give any person who may be affected by the order, as well as ASIC, an opportunity to make submissions to it about the matter.[119] In terms of section 657A (3), the Australian Panel in exercising its powers under this section must consider a

[113] See Corporations Act 2001, section 657(A)(1).
[114] Corporations Act 2001, section 657C (3).
[115] Guidance note 4 and also E Armson "Judicial Review of Takeovers Panel Decisions" in *The Takeovers Panel and Takeovers Regulation in Australia* (2010) 176-210.
[116] Guidance note 1 provides examples of unacceptable circumstances. See also Khan "Unacceptable Circumstances in Takeovers" **(**2010) 6 *MLJ,* discussing the Australian Takeovers Panel guidance note 1.
[117] Guidance note at para 17.
[118] E Armson "Models for Takeover Dispute Resolution: Australia and the UK" (2005) 5 Part 2 *Journal of Corporate Law Studies* 408*.*
[119] See Section 657A of the Corporations Act 2001.

number of other factors in addition to the principles relating to regulations of mergers and takeovers as set out in section 602. It must also observe other matters specified under the regulations made in terms of the ASIC Act.[120] The Panel rules provide detailed procedures and guidelines on how to lodge applications, including the format of the application, parties to whom documents must be provided, submission of confidential documents and withdrawal of applications.[121]

The guidance note indicates, that the Panel does not seek to punish when deciding on a remedy, although such a remedy may adversely affect a person.[122] The declarations are wide and could be orders in favour of any person whose interests are affected by the relevant circumstances. The Panel may also make any order, including remedial orders. These may include: an order to protect rights or interests of a person or group of persons in takeovers or mergers;[123] orders freezing transfer of securities proceeds; and orders freezing rights attached to securities.[124] Following a declaration, the Panel may also admonish any person including advisers, report such persons to relevant authorities or make media releases in respect of unacceptable circumstances.[125] Further, it may make cost orders against any person to pay costs of the hearing.[126] Subject to informing the affected parties, the Australian Panel may vary, revoke or suspend any order.[127]

In terms of section 657EA of the Corporations Act 2001, another Australian Panel may internally review matters that have been dealt with by a particular

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[120]See section 657A(3)(iv) Corporations Act 2001. Some of the matters relate to the procedures to be followed when making decisions.
[121]See Australian Takeover Panel, *Procedural Rules* (2010) paragraphs 1-10.
[122]See Australian Takeover Panel, *Guidance Note 4 Remedies General issue* (2017) paragraph 5.
[123]See Australian Takeover Panel, *Guidance Note 4: Remedies General issue* (2017) paragraph 2.
[124]See Australian Takeover Panel, *Guidance Note 4: Remedies General issue* (2017). paragraph 22.
[125]See Australian Takeover Panel, *Guidance Note 4: Remedies General issue* (2017) paragraph 49.
[126]See Australian Takeover Panel, *Guidance Note 4: Remedies General issue* (2017) paragraph 25.
[127]See rule 8 Australian Takeover Panel, *Procedural Rules* (2010).

Australian Panel; subject to a number of requirements including avoidance of conflicts of interests. In terms of section 657EB of the Corporations Act 2001, a court hearing a matter in relation to a decision of the Australian Panel could, instead of making a decision, refer the matter to the Australian Panel for review. The review panel has the same powers as the initial Australian Panel and considers the matter as if it has never been considered or heard before.[128]

Following section 602 of the Corporations Act 2001, dealing with the fundamental principles for regulating takeovers and mergers, and guidance note 1, dealing with 'unacceptable circumstances' may be explained under the following subheadings:

(a) Inhibition of efficient, competitive and informed markets

Section 602 of the Corporations Act 2001 requires that a takeover or merger must occur in an efficient, competitive and informed market. Accordingly, any circumstance in a takeover or merger that could have the effect of preventing the realisation of these principles should be declared unacceptable.[129] An unacceptable circumstance may result due to the deficiency of the information relating to the merger or takeover, the creation of a false market. Lack of sufficient resources to pay the takeover or merger price by the bidder may inhibit an efficient market for the shares of the target. Other circumstances that may result in unacceptable circumstances may be anti-takeover defences adopted by target companies, such as a high amount of a break fee[130] payable. A high amount of a break fee payable when the takeover or merger is not supported that is included in the takeover or merger agreement, may have the

[128]Rule 3.3 of the Australian Takeover Panel *Procedural Rules* (2010) and notes thereunder.
[129]Guidance note 1 issued by the Australian Takeovers Panel and the Notes there under; and see also Khan (2010) 6 *MLJ* **"**Unacceptable Circumstances in Takeovers" clvii-clxiv.
[130]A break fee refers to a fee usually payable by the target company (whose directors have agreed to support a negotiated acquisition transaction by the bidder) to a bidder if the transaction is not implemented in accordance with the agreed terms as a result of certain clearly defined events. See JC Coates, & G Subramanian, (2000) *Harvard Law School John M. Olin Center for Law, Economics and Business Discussion Paper Series.* Paper 274. Available on http://lsr.nellco.org/harvard_olin/274.) (Accessed 15 -12 -2017). It is also called other names including an "inducement fee." See also note 280 in chapter 2 in paragraph 2 5 2 above.

effect of discouraging a competing bid. Hence, an unreasonably high break fee may be declared unacceptable.[131] In the case of a no-talk shop agreement, the effect may be that directors are unable to seek competing bidders for the target company thereby preventing a competitive price for the target shares. This may be detrimental to target shareholders as they are then faced with one bid only.

The reuse of reports obtained for different purposes can also lead to misinformation in cases where it is not clear for whom, and for what purposes, the report was obtained. It is suggested that where the report was obtained for a certain purpose and then used to possibly support or to justify a merger, it may also be misleading. To counter this, it is a requirement that any report must be dated and provide certain prescribed information. This is aimed at preventing use of old and outdated reports or event reports which are not relevant to the particular takeover or merger.[132]

There must be a balance between the ability of directors to pursue transactions to maximise the interests of the company and the right of the shareholders to be able to consider the takeover bid.[133] In the matter of *Glencore International AG v Takeovers Panel,*[134] the Australian Federal Court described the process leading to the declaration of unacceptable circumstances by the Australian Panel.[135] The court also indicated that courts should be slow to interfere with the decision of the Panel as they are made in "circumstances where the market is significantly volatile by reason of the currency of takeover offers."[136] According to the court, the Australian Panel may declare circumstances unacceptable where it appears that particular circumstances are unacceptable due to the effect of these circumstances. The court pointed out that the Australian Panel has a duty to enquire and make a determination as to the effect of those circumstances.[137] Only the unacceptability of the effect will allow

[131]Khan (2010) *MLJ.* clxii-clxiii.
[132]Khan (2010) *MLJ* clix-clxiii.
[133]Khan (2010) *MLJ* clxiii.
[134]2005 FCA 1920.
[135]2005 FCA 1920 paras 30-32.
[136]2005 FCA 1920 para 35.
[137]2005 FCA 1920 paras 38-39.

intervention by the Australian Panel. The Australian Panel must first make a finding about the existence of unacceptable circumstances. It would then determine its effect on a merger or a takeover. The court referred to section 657A (2) of the Corporations Act 2001 and stated that the Review Panel in this matter was required to make a finding that the circumstances will have some effect on either the acquisition or control as referred to in section 657A (2).[138] Following the judgment, the powers of the Panel was further clarified as discussed under paragraph 4 3 below.

(b) Details and identity of the bidder

The shareholders and the directors of a company must know the identity of a person who proposes to acquire a substantial interest and must be given a reasonable time to consider the proposal. Furthermore, they must be given enough information to enable them to assess the merits of the proposal.[139]

(c) Misinformation relating to the bid

Misinformation and misleading information may result in unacceptable circumstances due to the fact that shareholders will not receive the relevant information to make an informed decision. Disclosure of the relevant information is therefore important to enable shareholders to consider the merits and demerits of an offer. Information contained in shareholder circulars, bidder statements and independent expert advisers must comply with the Corporations Act 2001 and its regulations.[140]

(d) Reasonable and equal opportunities to consider the offer

It is a fundamental principle in takeovers and mergers that shareholders be offered a reasonable and equal opportunity to be able to take part in the benefits

[138] 2005 FCA 1920 paras 38-39.
[139] See guidance note 1 and the Notes there under; and also, in Khan (2010) *MLJ* clix.
[140] Guidance note 1 and also Khan (2010) MLJ, clvi-clvii.

of an offer or a transaction which result from a change of control.[141] As the guidance note states, reasonableness relates to the ability of shareholders to have enough time to consider, sell or vote if required. The guidance note further states that shareholders should not be subjected to pressure tactics to accept the offer. Shareholders should have a reasonable opportunity to participate in the offer.[142] This requirement does not mean that the offer must be equally acceptable to all shareholders. It only means that the offer is made to all shareholders equally, while some may find the offer more attractive than others due to their peculiar circumstances or the price they paid for their shares.[143]

(e) Appropriate procedure for compulsory acquisition of voting shares

Another requirement introduced by section 602 of the Corporations Act 2001 is that there must be a suitable avenue to allow shareholders to exit or sell their shares to the controllers once the controlling shareholders have reached levels of acceptance beyond 90 percent of the issued shares of the company. This is intended to prevent shareholders from being trapped in a company without any means of selling their shares in cases where they remain as minorities. At the same time, it also avoids shareholders greenmailing controlling shareholders by demanding unreasonable compensation for their shares.[144]

(f) Examples of unacceptable circumstances

According to the various guidance notes, examples of possible unacceptable circumstances include: a bidder not having funding in place to pay to the takeover,[145] actions that may result in frustrating of a takeover bid,[146] a target company's associate acquiring the target's shares as a defense to a takeover

[141]See section 602 Corporations Act 2001.
[142]See section 602 Corporations Act 2001.
[143]See Ramsay "The Takeovers Panel: A Review" in *The Takeovers Panel and the Takeovers Regulation in Australia* 8.
[144]See guidance note 1 and also Australian Securities Investment Commission, Corporate control: a better environment for productive investment Corporate Law Economic Reform Program Proposals for Reform: Paper No. 4 1997 Available at: http, (Accessed 14-2-2014).
[145]See Guidance Note 14 Funding Arrangements.
[146]See Guidance Note 12 Frustrating Action.

bid,[147] rights issues undertaken by the target company that are not readily available to all shareholders[148] and payments of collateral benefits to other shareholders.[149]

4 2 5 The Australian Takeover Panel's powers to enforce and prohibit transactions

In order to bolster enforcement of the above requirements and to discourage noncompliance, the Corporations Act 2001 in section 606 prohibits certain acquisitions unless such acquisitions have been exempted or allowed by ASIC. This is the 'central prohibition' in Australian takeover provisions as discussed in paragraph 4 2 2 above.[150] These prohibitions are aimed at achieving the policy objectives set out in chapter 6 of the Corporations Act 2001. In terms of section 606 of the Corporations Act 2001, there is a clear, outright prohibition on making an offer that would mean that the purchaser would hold 20 percent or more of the issued shares of a company or similar instruments, or any further percentage up to 90 percent of the issued shares of a company or similar instruments. The emphasis is on voting shares or relevant interest or equity in an Australian company or a body corporate. The various concepts, such as the company, body corporate, voting shares, relevant interests or equity are all clearly defined in the Corporations Act 2001. Any acquisition or the making of an offer to acquire the relevant interests which would result in a contravention of subsection 606 of the Corporations Act 2001, is similarly prohibited in terms of section 606 (4) of the Corporations Act 2001. The Australian legislature considered it imperative that the various concepts are clarified. It is suggested that this was done to avoid any uncertainty or vagueness in relation to the interpretation of the various concepts. It is asserted that clarity and certainty is important in order to ensure effective and efficient enforcement of takeovers and merger provisions.

[147] Guidance Note 7 Lock-up devices.
[148] Guidance Note 17 Rights Issues.
[149] Guidance Note 21 Collateral Benefits.
[150] The Eggleston Principles are incorporated in section 602 of the Corporations Act 2001. See also the discussions by Armson (2009) *Melbourne University Law Review* 659.

To ensure that there is no avoidance of the prohibitions in section 606 of the Corporations Act 2001, the prohibitions are couched broadly. They cover any acquisitions of relevant interests in voting securities. The exemptions, and allowed acquisitions include:

- acquisition transactions that results from acceptance of an offer under a takeover bid;
- acquisitions in relation to bid class securities that result from an on-market bid;
- acquisitions of a bid class that results directly from the exercise of rights attached to convertible securities during a takeover bid;
- acquisitions that results from the exercise by a person of power, or appointment as a receiver, or a receiver, manager under a mortgage;
- acquisitions approved previously by a resolution passed at a general meeting of the company in which the acquisition is made;
- acquisitions resulting from the issue of securities of the company in which the acquisition is made if the company has started to carry on any business and has not borrowed any money;
- acquisitions that result from another acquisition of the relevant interests in voting shares in a body corporate included in the official list of a prescribed financial market or a foreign body conducting a financial market that is a body approved in writing by ASIC; - acquisitions made through a will or through the operation of law,
- acquisition made through a compromise or arrangement approved by a court;
- acquisition that results from an arrangement entered into by a liquidator; and;
- acquisition that results from a buyback authorised by section 257A of the Corporations Act 2001.

The Australian Panel also has the power to make any order that it deems appropriate in order to protect the interests of any person affected by unacceptable circumstances. This ensures, where possible, that a takeover bid proceeds as if the unacceptable circumstance had not occurred. This may take the form of an interim order.[151] In addition, the Australian Panel may also review

[151]See Guidance Note 4- Remedies General at paragraph 10.

the decisions made by ASIC in respect of a takeover or a merger during a bid period. Another power of the Australian Panel is that it could accept undertakings for the purposes of settling unacceptable circumstances during a takeover or merger where it considers that it is in the public interest.[152] The Australian Panel may order additional disclosures, cancellation of contracts, freezing of transfers of securities, freezing of transfers of rights attached to securities, which forces the disposal of securities and allow more time to provide additional information or establish rights of withdrawal.[153] The Australian Panel in exercising its powers must balance different interests. Therefore, it weighs the rights or interests of all persons involved against the possible prejudice that may result from making or not making an order.[154]

4 2 6 A brief overview of Australian Panel proceedings during hearings

The Australian Panel operates like a court in an adversarial setting.[155] However, the procedures followed by the Australian Panel differ markedly from that of a court. For example, unlike the courts, the Australian Panel is not bound by rules of evidence or by precedents.[156] The main aim of Australian Panel procedures is that of efficiency and fairness. In terms of efficiency, the Australian Panel prefers that matters be dealt with in writing, rather than by means of oral presentations or arguments. This is because dealing with matters on paper is often found to be expeditious and quicker. This allows the Australian Panel to consider applications within a shorter period than would be the case if the parties would appear personally before the Australian Panel in a hearing.[157] Another important requirement for the proceedings of the Australian Panel is that of fairness. Fairness requires that parties have to be able to make submissions and that the proceedings must be fair. Hence, parties are allowed

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[152]Ramsay "The Takeovers Panel: A Review" in *Ramsay (ed) The Takeovers Panel and the Takeovers Regulation in Australia* 9.
[153]Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 51.
[154]51.
[155]Armson (2004) *Melbourne University Law Review* 565.
[156]565.
[157]565.

to exchange submissions and are entitled to receive responses to all applications and all other papers submitted to the Australian Panel in support of the applications.[158]

The Australian Panel rules were published in accordance with section 188 of the Australian Securities Investment Commission Act 2001 and contain procedural rules for all hearings before the Australian Panel.[159] The rules make provision for, among others, regulations regarding applications to the Australian Panel, referral of matters to the Australian Panel, the time period for proceedings, abuse of Australian Panel proceedings, decisions made by the Australian Panel to conduct proceedings, requests by parties to be involved in proceedings, conduct of conferences, purposes of conferences, witnesses, misbehaviour by parties and summons for witnesses, and payment of expenses of parties involved in proceedings. The Australian Panel procedural rules specifically state that their objectives are to promote:

> "(a) procedural fairness;
> (b) timely and cost-effective completion of proceedings;
> (c) obtaining the best available information and
> (d) not unnecessarily delaying commercial transactions."[160]

Rule 10.2,[161] indicates that the rules are to be interpreted according to their spirit, by looking beyond form to substance and in a way that best promotes the objectives set out in paragraph (a) to (d) above. The rules are made by the president of the Australian Panel in consultation with other members of the Australian Panel. The rules must take into consideration the purposes of chapter 6 as set out in section 602 of the Corporations Act 2001.[162]

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[158]565.
[159]Australian Takeovers Panel, Panel Proceedings, Available at: http//www.takeovers.gov.au. content/rules_for_proceedings/ default.aspx, (Accessed on 15-2-2014).
[160]Australian Takeovers Panel, Procedural Rules, Rule 10.1 Definitions and interpretations.
[161]Australian Takeovers Panel, Procedural Rules, Rule 10.2 Definitions and interpretations.
[162]Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 69.

4 3 A brief evaluation of the Australian Panel's functions and performance

It has been generally accepted by most commentators that, prior to the amendments brought about by the CLERP reforms, the Australian Panel was not successful in its role as a regulator of mergers and takeovers.[163] The debate on the successes of the Australian Panel continues. The key criterion in measuring the successes of the Australian Panel is the number of transactions that have been regulated by the Australian Panel as compared to the earlier period.[164] The period after the promulgation of the CLERP provisions saw dramatic changes on how the Australian Panel operated, and the Australian Panel is now highly regarded as a successful regulator. It is important to identify the reasons why the Australian Panel became so successful in takeover dispute resolution.[165] Various reasons have been mentioned for its successes. The reasons for the successes of the Australian Panel are numerous and include the independence of the Australian Panel and the fact that the Australian government strengthened the role of the Australian Panel in takeovers disputes.[166] Making the Australian Panel the main adjudicator of takeover disputes during the course of a takeover did this.

The earlier takeover provisions limited the role of the Australian Panel to only being able to react to referrals from ASIC.[167] The amendments brought about by the Corporations Act 2001 enabled parties to approach the Australian Panel directly for resolution of takeover disputes, and the decision of the Full Federal Court in the *Alinta Ltd* case[168] confirmed the constitutional validity of the Australian Panel. The fundamental question in the *Alinta* case was whether the

[163] Calleja *The New Takeover Panel –A Better Way?* 4; See also McKeon "Foreword" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* vi; See also Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1.
[164] Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1-38.
[165] See Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1-38.
[166] See Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1-38.
[167] See paragraph 4 2 2 on developments of takeover and merger provisions in Australia.
[168] (2008) 233 CLR 542 16.

Australian Panel exercised judicial powers contrary to the requirements of the Commonwealth Constitution, which prevented the Australian Parliament from "reposing any power essentially judicial in any other organ or body" other than the courts.[169] One of the key reasons why the Federal Court upheld the constitutional validity of the Australian Panel was that the Australian Panel's powers were underpinned by policy.[170] The Australian Panel is not exercising judicial powers in declaring unacceptable circumstances, because those circumstances constitute contravention of the Corporations Act 2001.[171]

By declaring the powers of the Australian Panel constitutionally valid, the courts removed any skepticism that had earlier plagued the Australian Panel's proceedings.[172] The breadth of the Australian Panel's powers was also confirmed by the Full Federal Court in *CEMEX Australia Pty Ltd v Takeovers Australian Panel,*[173] dealing with the powers of the Australian Panel to declare unacceptable circumstances. While there may still be challenges to the Australian Panel's powers, the legislative framework is now robust and the courts accept the Australian Panel as the primary regulator in takeovers on the basis of "commercial, policy and public interest factors".[174]

Another feature of the Australian Panel's' structure which led to its success is the clearer delineation of the respective roles of the courts and the Australian Panel. Where it appears that there is uncertainty as to the role of the Australian Panel, this is bound to affect the credibility of the Australian Panel.[175] The strength of the membership of the Australian Panel also contributes to its achievements: The fact that members of the Australian Panel are industry professionals allows the Australian Panel to enjoy greater respect and

[169]Armson "Judicial Review of Takeovers Panel Decisions" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia*.188.
[170]Armson (2009) *Melbourne University Law Review* 659.
[171]659.
[172]Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 6.
[173](2009) 257 ALR 403.
[174]Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 61-62.
[175]Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 16.

credibility. [176] It can be argued that this is due to the fact that participants often have to face their peers in a different environment as regulators. The influence of the Australian Panel on market practice is also important for the success of the Australian Panel: As the Australian Panel started providing guidelines on takeovers and making more decisions, it developed consistent and accepted market behaviour.

The Australian Panel also influenced acceptable market practices by issuing guidelines along with its decisions.[177] The speed with which the Australian Panel makes decisions also contributed to its success: The fact that the Australian Panel could make timely decisions, led to market participants gaining confidence in the ability of the Australian Panel. The Australian Panel was able to make decisions much more speedily than the courts.[178] The accessibility of the Australian Panel also contributed to its success: By keeping its doors open, it encouraged participants to consult them and seek guidance.[179] Furthermore, the new provisions facilitated a shift away from tactical litigation. Prior to the amendments brought about by the Corporations Act 2001, the Australian Panel was beset by tactical litigation.[180]

The Australian Panel's extensive consultation processes are yet another factor contributing to its success. By consulting practitioners, the Australian Panel ensures that market participants buy into its decisions.[181] It is suggested that participants readily cooperate and easily abide by market practices and rules that they had a part in forming and implementing. The Australian Panel's informal and non-legalistic approach to resolving takeover disputes is also credited for its achievements. The informal nature of the dispute resolutions also encouraged people who are not lawyers to readily approach the Australian Panel and thereby facilitated speedy decision-making.[182]

[176] 18.
[177] 19.
[178] 20.
[179] 22.
[180] 23.
[181] 25.
[182] 27.

The Australian Panel's focus on policy is also responsible for its success:[183] Focusing on and adhering to policies underlying the regulation of takeovers and mergers, which is to protect investors, ensures that the Australian Panel does not shift from its mandate. The support the Australian Panel has received from the government, in the form of monetary support and assistance, enables the Australian Panel to properly carry out its mandate. It is doubtful whether the Australian Panel would have been so successful without proper government support.[184]

Finally, the effective leadership of the president of the Australian Panel, and the expertise of the Australian Panel executive, has played a major role in the achievements of the Australian Panel so far. Experienced Australian Panel executives who advised parties about Australian Panel rules and procedures also played a crucial role in practitioners gaining confidence in the Australian Panel.[185] In order to promote compliance with the takeover provisions, the Australian Panel has issued a number of guidance notes. Some of the most important guidance notes includes Guidance Note 1, which is intended to assist market participants to understand the Australian Panel's approach to making a declaration of unacceptable circumstances as discussed in paragraph 4 2 4 above. It provides an overview of the Australian Panel's powers and the circumstances in which the Australian Panel may declare circumstances unacceptable.

Guidance Note 7, indicates that certain terms and conditions of takeovers such as break fees and no talk shop agreement, that may result in unacceptable circumstances are not allowed, as discussed in paragraph 4 2 4 above. Some of these terms and conditions, may discourage competitive bids, to the detriment of shareholders. Whether such terms and conditions are considered unacceptable in relation to a takeover bid will depend on their effect on the general principles set out in section 602 of the Corporations Act 2001, the main

[183] 29.
[184] Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia*, 30.
[185] 30.

principles relating to protection of shareholders during takeovers or mergers. Should a term or condition of a takeover or merger be found to have a negative effect on the principles set out in section 602, it may be declared unacceptable.

Guidance Note 12 deals with frustrating actions on bids. In terms of this guidance note, directors may not take any action that could have the effect of defeating or frustrating a takeover bid. Guidance Note 18 deals with the details and content of takeover documents. Guidance Note 21 covers payment of collateral benefits that may be declared unacceptable in relation to a takeover bid.[186]

ASIC[187] has more recently issued Regulatory Guide 9 - Takeover Bids. ASIC points out that the guide was issued to companies, their advisers and investors, and

> "[D]iscusses ASIC's regulatory role in relation to takeover bids and how we interpret and administer the requirements of the takeover provisions in Chapter 6 of the *Corporations Act 2001* (Corporations Act); and explains how we exercise our discretionary powers in relation to takeover bids, including the power to exempt from, or modify, the takeover provisions. "[188]

An empirical study by Armson indicates that the highest number of applications to the Australian Panel relates to the provisions of chapter 6 of the Corporations Act 2001.[189] This is not surprising due to the fact that the fundamental principles of the takeover provisions are contained in section 602 of chapter 6 of the Corporations Act 2001. In conclusion she states that in the first five years the Australian Panel focused significantly on the purpose of an "efficient, competitive and informed market" and the substantive requirements relating to the takeover procedures and offers under chapter 6 of the Corporations Act

[186]Australian Takeovers Panel. Guidance Note 21. See paragraph 4 2 4 above discussing how the Panel deal with unacceptable circumstances in takeovers.
[187]ASIC. Regulatory Guide 9: Takeover bids. Available at: http://www.asic.gov.au.(Accessed on 14-2-2014).
[188]ASIC. Regulatory Guide 9: Takeover bids.
[189]Armson (2005) *Sydney Law Review* 665.

2001.[190] She further indicated that it is not surprising that the majority of the decisions of the Australian Panel involve matters relating to disclosures in takeovers that had been declared unacceptable.[191]

Miller, Campbell and Ramsay[192] undertook another empirical study aimed at providing an understanding of how, and with what degree of effectiveness, the Australian Panel has operated since the amendment brought in by the Corporations Act 2001. The study analysed some 153 matters that were considered and decided upon by the Australian Panel between May 2000 and January 2005. The most popular remedy sought by applicants was a declaration of unacceptable circumstances in terms of section 657A, which constituted 73 percent of all the applications. Section 636 deals with the content of bidder's statements and is one of the common sections to be contravened. The majority of the applications involved small capitalisation companies. This suggests that takeover transactions involving small capitalisation companies are the most problematic.[193]

Despite the achievements of the Australian Panel post CLERP reforms, some commentators believe that additional reforms will assist the Australian Panel to offer better oversight role for takeovers and mergers. Levy & Pathak have made comprehensive proposals to enhance the regulatory oversight role of the Australian Panel.[194] The views and proposals for reform include that disputes could be resolved quickly if the Panel had full-time members.[195] It is also suggested that tactical litigation has shifted from the courts to the Australian Panel.

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[190]673.
[191]673.
[192]C Miller, R Campbell & Ramsay I *The Takeovers Australian Panel: An Empirical Study* (August 2006). University of Melbourne Legal Studies Research Paper No. 160. Available at: http://ssrn.com/abstract=924501> or <http://dx.doi.org/10.2139/ssrn.924501 (Accessed 14-2-2014).
[193]See Miller, Campbell & Ramsay *The Takeovers Australian Panel: An Empirical Study* (2006) 32.
[194]R Levy & N Pathak "The Takeovers Panel of the Future" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 211-240.
[195]216.

The practice where interested parties review the bidder statement and then raise objections by applying to the Australian Panel, seeking changes or additional disclosures, has the same effect as delaying the transaction in court applications.[196] The proportion of hostile offers ending up at the Australian Panel may be the same as those that ended up in the courts.[197] Factors that encourage tactical litigation at the Australian Panel include absence of punitive costs awards, the relatively inexpensive nature of Australian Panel proceedings and the absence of powers to award damages.[198]

It has further been suggested that the powers of the Australian Panel should be enhanced.[199] The Corporations Act 2001 should be amended to reduce uncertainty in respect of the scope of the Australian Panel's jurisdiction relative to that of the courts. While the Panel is the main forum during takeovers, it is not the exclusive forum.[200] There is an overlap between the jurisdiction of the courts and that of the Panel.[201] The law is not clear on whether there is a possibility for parties to 'forum shop' and whether both the Australian Panel and the court may have jurisdiction to hear a matter.[202] It is also suggested that the Australian Panel should be given additional powers. These would include the power to make advance rulings, the power to grant exemptions and modifications, the power to excuse contraventions and the power to intervene directly in a takeover rather than wait for the parties to lodge an application.[203]

Currently, the Australian Panel has no powers to regulate schemes of arrangements.[204] This is a 'significant gap.'[205] The current schemes of arrangements provisions are complex, as they require assessment of a large

[196] 217.
[197] 217.
[198] 217.
[199] 222-231.
[200] 222.
[201] 222.
[202] Levy & Pathak "The Takeovers Panel of the Future" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 222.
[203] 231.
[204] Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 63.
[205] 70.

body of case law.[206] The current schemes of arrangement should be simplified before the authority to regulate such methods is shifted to the Australian Panel.[207] There should be a single regulator with specialist expertise in the two methods of bringing a change in control in companies[208]

Finally, it has been proposed that resources of the Australian Panel should be increased by, for example, expanding the executive of the Australian Panel and adding a full-time president to the Australian Panel and applying a modified UK Panel model of using merchant bankers and lawyers who have been seconded by their institutions for a year. The seconded lawyers and bankers should form part of the sitting Australian Panel and be involved in hearing matters.[209] Cash funding should also be increased for the Australian Panel and the methods of funding the Australian Panel should be reconsidered.[210] Cost orders should be increased to discourage trivial complaints and applications. Applicants could also be made to defray the costs of the Panel.[211] Application fees should be increased and some of ASIC's funding should be made available to the Australian Panel.[212]

4 4 Concluding remarks

It is suggested that the rationale for Australian authorities not adopting UK takeover laws wholesale was that they had considered that Australia has a different economy, markets, companies and regulatory environment than the UK. Therefore, they had to create new takeover rules to suit their own context instead of transplanting UK takeover laws wholesale.[213] This was despite the strong historical connection between the two countries in, notably, their culture,

[206]Levy & Pathak "The Takeovers Panel of the Future" in *Ramsay (ed) The Takeovers Panel and Takeovers Regulation in Australia* 227.
[207]228.
[208]227.
[209]234-235.
[210]236.
[211] Levy & Pathak "The Takeovers Panel of the Future" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 237.
[212]236.
[213]Thompson (2002) *Vanderbilt University Law School Law & Economics Working Paper Number* 02-26, 2.

economies, markets and company laws.[214] In introducing the various reform policies, such as the Eggleston Principles, as the fundamental principles for regulating takeovers and mergers, it is suggested that the authorities deliberately acknowledged that Australia needed a unique approach to takeover regulation. Even though the mandatory offer was considered, it was not adopted. [215] Australia has combined aspects of the UK's takeover regulatory regime with unique Australian aspects.[216] As indicated above, in paragraph 4 2 2, the equal treatment rules in Australia are more stringent than those of the UK City Code even though Australia does not have a mandatory offer.[217]

The Australian Panel faced a number of difficulties in its initial years of operation. The difficulties are attributed to a number of factors, which have since been resolved. The reformed Australian Panel has made commendable strides, as can be seen by a number of positive comments from various commentators.[218] The Australian Panel now enjoys the respect and confidence of those who are actively involved in takeovers following a number of reforms undertaken.[219] It is not possible to compile a common list of factors that have led to the success of the Australian Panel. Scholars have highlighted that the Australian Panel regulates according to "the spirit, rather than the letter of the law".[220] The Australian Panel is an independent regulatory body, with part time members appointed from the active members of Australia's takeovers and business communities. Its efficiency has also led to market participants gaining confidence in its dispute regulatory activities. It appears that, despite criticism

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[214]1-2.

[215]See Armson (2012) *Monash University Law Review* 683 at note 252.

[216]See A Dignam tThe globalisation of General Principle 7: transforming the market for corporate control in Australia and Europe" (2008) *Legal Studies* 96al St

[217]J Mannolini '*Convergence or Divergence: Is there a Role for the Eggleston Principles in a Global M&A Environment* '(2002) Vol 24:336 *Sydney Law Review* 358.

[218]I Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1-38; Hoyle "An Overview of the Role, Functions and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 39-79; Levy & Pathak "The Takeovers Panel of the Future" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 211-240.

[219] Ramsay "The Takeovers Panel: A Review" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 1-38.

[220]See also rule 10 of the Takeover Panel Procedural Rules and Dyer & MacDonald "Why Was the Takeovers Panel Established" in Ramsay (ed) *The Takeovers Panel and Takeovers Regulation in Australia* 81.

by some researchers, the Australian Panel continues to operate successfully upholding policy considerations for regulating takeovers and mergers.

There are a number of similarities in the takeover rules of the UK and Australia. However, there is a clear distinction in the content and the manner in which the rules are applied. These similarities and distinctions will be discussed in chapter 6 below, which evaluates the takeover and merger provisions of selected countries.

Chapter 5: An overview of the regulation of takeovers and mergers in South Africa with an emphasis on the mandatory offer

"It is respectfully submitted that South African corporate law is in dire need of reform. The imperative of globalisation is that domestic regulation of any country cannot be allowed to be out of step with international trends, each country's domestic laws must be investor friendly in order to attract foreign investors. The South African corporate legislation is defective in a number of respects and in this regard, attention must be drawn to the archaic provisions relating to capital maintenance."[1]

5 1 Introduction

Having reviewed takeovers and mergers provisions from comparative countries, this chapter discusses the South African provisions in detail. Of the three comparative countries analysed in the dissertation, the South African takeover and merger provisions are the most recent. In trying to keep up with the developments in other countries, South Africa had its company law entirely revamped. The takeover and merger provisions of the Companies Act 61 of 1973 (Companies Act of 1973) in the form of the SRP Code were comprehensively amended to form part of Chapter 5 of the Companies Act of 2008 as discussed in Chapter 1 (the Takeover Provisions). The new provisions generally adhere to the structure of the existing South African company law, while adding new provisions borrowed from other jurisdictions, such as the US.[2]

In her research, Luiz comprehensively discusses the SRP Code on takeovers and mergers that has now been replaced by chapter 5 of the Companies Regulation 2011 (Takeover Regulations), effective May 2011.[3] Her research

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[1]MM Katz "Developments in corporate law" *Journal for Juridical Science (*1997) 22(2).39.
[2]E Davids, T Norwitz & D Yuill "A Microscopic analysis of the new merger and amalgamation provision in the Companies Act 71 of 2008" (2010) *Acta Juridica* 338.
[3]S Luiz *An evaluation of the South African Securities Regulation Code on Takeovers and Mergers* LLD Thesis, Unisa (2003) 573-1022.

traces the history of the regulation of takeovers and mergers in South Africa. The SRP Code was modelled on English company law.[4] The UK Code was, until recently, a form of self-regulation.[5] The approach to regulation of takeovers and mergers of self-regulation, in line with the UK practice, was adopted by the South African legislature when it introduced the SRP Code even though the SRP Code was based on statute.[6] In the introduction and explanatory note of the SRP Code, it is stated that “the appointment of the Panel and its formulation and application of the rules in the Code, express the principle of self-regulation by the securities industry”. The Takeover Regulations have been based on the SRP Code,[7] which in turn was based on the UK City Code on Takeovers and Mergers, commonly referred to as the City Code.[8] The fact that SA company law originated from UK company law may have played a pivotal role in the adoption of the City Code. In addition, SA and the UK’s close economic ties may also have contributed to the adoption of the UK City Code.

5 2 Objectives of the Companies Act of 2008 in respect of takeovers and mergers

It is submitted that the Companies Act of 2008 has finally brought the South African company law in line with modern corporate law practice of other countries. It was generally accepted that the Companies Act of 1973 was outdated. The Companies Act of 2008 repealed the Companies Act of 1973, and introduced comprehensive changes to South African company law. According to the DTI 2004 Policy document, the Companies Act of 2008 seeks to make company law simple, flexible, transparent, predictable and efficient. The document indicates that the Companies Act of 2008 is aimed at ensuring:

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[4]Luiz *An Evaluation of South African Securities Regulation Code* 573-1022.
[5]See also Johnston “Takeover Regulation: Historical and Theoretical perspectives on the City Code” *Cambridge Law Journal* (2007) 66:2, 447.
[6]Securities Regulation Code (SRP Code) and the Rules of the Securities Regulation Panel (SRP). Government Gazette12962. January 1991.
[7]See Introduction and the explanatory notes to the SRP Code.
[8]See Part B and C of Chapter 5 to the Companies Act of 2008 and the regulations thereto. Some of the sections of the Act read very similar to the repealed SRP Code rules. See for instance section 126 of the Companies Act of 2008 and compare it to rule 19 of the SRP Code.

> "[T]hat the regulatory framework for enterprises of all types and sizes promoted growth, employment, innovation, stability, good governance confidence and international competitiveness. Regulation should be consistent, effective, predictable, transparent, fair and understandable. It should provide flexibility and promote adaptability to an environment with fast changing technologies, economic opportunities and social circumstances. The regulatory scheme should not create artificial preferences and distortions, where these are unnecessary. And it should attempt, where practically possible, to balance the competing interests of economic actors and of society at large."[9]

In the DTI 2004 Policy document, it was acknowledged that the existing takeovers and mergers regulations applied by the SRP, in the form of the SRP Code,[10] were aligned with international practices. However, it was also accepted that there was a need to review the enforcement measures of the SRP to ensure compliance with the SRP Code.[11]

The DTI 2004 Policy document, explained the need to rewrite the Companies Act of 1973, as follows:

> "It is not the aim of the DTI simply to write a Companies Act 2008 by unreasonably jettisoning the body of jurisprudence built up over more than a century. The objective of the review is to ensure that the new legislation is appropriate to the legal, economic and social context of South Africa as a constitutional democracy and open economy. Where current law meets these objectives, it should remain as part of company law."[12]

In its preamble, among other things, the Companies Act of 2008 indicates in respect of takeovers and mergers that it seeks "to provide for equitable and efficient amalgamations, mergers and acquisitions of companies".[13] The DTI

[9]DTI 2004 Policy document 9.
[10]DTI 2004 Policy document 40.
[11]DTI 2004 Policy document 41.
[12]DTI 2004 Policy document 7.
[13]Preamble to the Companies Act of 2008 as amended.

2004 Policy document rests on five objectives.[14] These objectives are named as:

> "(1) to simplify the procedure for company formation and reduce the costs of forming and maintaining a company;
> (2) to promote flexibility in the design and organisation of companies and to ensure a predictable and effective regulatory environment;
> (3) to promote the efficiency of companies and their management;
> (4) to encourage transparency and high standards of corporate governance;
> (5) to harmonise our company law with the best practice jurisdictions internationally."[15]

Section 7 of the Companies Act of 2008 also sets out the objectives of the legislature in enacting the new legislation. The objectives are: (a) promoting compliance with the Bill of Rights as provided in the Constitution when company law is applied; (b) promoting the development of the South African economy by (i) encouraging entrepreneurship and enterprise efficiency, (ii) creating flexibility and simplicity in the formation and maintenance of companies, and (iii) encouraging transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation; (c) promoting innovation and investment in South African markets; (d) reaffirming the concept of the company as a means of achieving economic and social benefits; (e) providing for the creation and use of companies in a manner that enhances the economic welfare of South Africa as a partner within the global economy; (f) promoting the development of companies within all sectors of the economy, encouraging active participation in economic organisation, management and productivity; (g) create optimum conditions for the aggregation of capital for productive purposes and for the investment of that capital in enterprises and the spreading of economic risk; (h) balancing the rights and obligations of shareholders and directors within companies; (i) encouraging the efficient and responsible management of companies in a manner that balances the rights and interests of all relevant

[14]FHI Cassim "The Companies Act 2008: An Overview of a Few of its Core Provisions" (2010) 22 SA *Merc LJ* 158.
[15]Cassim (2010) SA *Merc LJ* 158.

stakeholders; and (j) providing a predictable and effective environment for the efficient regulation of companies.[16]

Takeovers and mergers involve risks for both shareholders and offerors. There are also inherent conflicts between different parties, including incumbent management. Therefore, it is important that their activities are properly regulated and the Takeover Provisions are aimed at realising this objective.[17] The Takeover Provisions should ideally strike a balance between the interests of all stakeholders of the company, including the economy and society at large.[18] It is suggested that some of the provisions of the Companies Act of 2008, such as, the mandatory offer requirement in section 123, prevent the realisation of some of the objectives set in the DTI 2004 Policy document and statute.

5 3 Authorities responsible for regulating takeovers and mergers

With the above objectives in mind, the Companies Act of 2008 has introduced a number of changes compared to the Companies Act of 1973. The Companies Act of 2008 in section 197 of chapter 5, creates, empowers and clarifies the role of the Panel,[19] a new body that replaced the SRP.[20] The Panel performs the same functions of regulating takeovers and mergers as the former SRP had done. The Companies Act of 2008 clarifies and enhances the functions and powers of the Panel. The new name clearly indicates what type of the transactions the Panel regulates and avoids any possible confusion that may have existed due to the reference to "securities" in the name of the former SRP. The reference to securities regulations is broader and may be confusing as the Financial Services Conduct Authority (previously the Financial Services Board) also undertakes the broader regulation of securities. The usage of Takeover

[16]See Section 7 of the Companies Act of 2008.
[17]S Luiz "Protection of holders of securities in the offeree regulated company during affected transactions: general offers and schemes of arrangements" (2014) 26 *Merc LJ.* 560.
[18]Davids et al (2010) *Acta Juridica* 337-338.
[19]Section 197 of the Companies Act of 2008.
[20]The SRP was created by section 440B of the Companies Act of 1973.

Regulation Panel more accurately reflects those aspects of securities relating to takeovers and mergers.

Section 197(1) of the Companies Act of 2008 provides for membership of the Panel. Members of the Panel consist of the Competition Commissioner (or a person designated by him/her) and the Companies Commissioner (or a person designated by him/her). Other members are appointed as follows: Three persons are designated by each exchange, and the Minister of Trade and Industry (the Minister) appoints additional members, based on "their knowledge and experience in the regulation of securities and takeovers."[21] SRP members appointed in terms of the Companies Act of 1973 continued as members of the Panel in accordance with the transitional provisions of the Companies Act of 2008.[22] Members appointed in terms of section 197(1) (a) and (b), being the Companies Commissioner and the Competition Commissioner respectively, serve on the Panel as long as they hold such offices. Those appointed in terms of section 197(1)(c) serve for a period of five years unless replaced earlier by the exchange. Members appointed in terms of section 197(1)(d) hold office for a period of five years.[23] The Panel may also co-opt additional members for a specific purpose and for a limited period.[24] The Minister may designate a chairperson and deputy chairpersons of the Panel from among members of the Panel. The Executive Director or the Deputy Executive Director and the employees of the Panel carry out the day-to-day operations of the Panel.[25]

The structure of the Panel and the appointment of Panel members differ from which existed in terms of the Companies Act of 1973. Under the Companies Act of 1973, a number of institutions and organisations were entitled to nominate members of the SRP, who were then appointed to the SRP by the

[21]Section 197(1) (d) of the Companies Act of 2008.
[22]Schedule 5(12) of the Companies Act of 2008 provides that the members of the old SRP will continue to hold office as members of the new Panel.
[23]Section 197(4) of the Companies Act of 2008.
[24]Section 197(2) of the Companies Act of 2008.
[25]Section 200 of the Companies Act of 2008.

Minister.[26] In terms of the Companies Act of 2008, the Minister plays an important role in deciding who is appointed as a member of the Panel.[27]

The Companies Act of 2008 also created a new body in terms of section 202(1), known as the Takeover Special Committee (TSC), which is a committee of the Panel. Members of the TSC consist of at least three persons.[28] The function of this body is to hear and decide on referrals made to it by the Panel and to review compliance notices issued by the executive director or deputy executive director of the Panel.[29] The Panel designates members of the TSC from time to time. The TSC is similar to the appeal committee of the SRP.[30] However, the appeal committee of the SRP was created in the SRP Code, which was subordinate legislation in terms of the Companies Act of 1973, whereas the TSC is created in the main legislation.[31]

The functions and the role of the TSC are similar to those of the old appeal committee of the SRP.[32] The quorum of the old SRP appeal committee was five members and it may have consisted of any member of the SRP, irrespective of the body or organisations that nominated him or her.[33] However, in the new TSC, only members appointed by the Minister in terms of section 197(1) (d) of the Companies Act of 2008 may be members of this committee.[34] In addition, section 202(2) of the Act specifically requires the chairperson of the TSC to be either an attorney or an advocate, whether practising or not.

[26]Section 440 B (3) of the Companies Act of 1973.
[27]Section 197(1) (d) of the Companies Act of 2008.
[28]Section 202(2) of the Companies Act of 2008.
[29]Section 202(3) of the Companies Act of 2008.
[30]SRP Code section 2(d).
[31]Section 440C of the Companies Act of 1973 and the SRP Code section 2(d).
[32]Section 202(3) of the Companies Act of 2008 and SRP Code sections A2(c) and A2 (d).
[33]SRP Code Section A 2 (d).
[34]Section 202(2) (b) of the Companies Act of 2008.

5 4 Functions of the Takeover Regulation Panel

Section 201 of the Companies Act of 2008 lists four functions of the Panel.[35] All these powers existed in the Companies Act of 1973 in one form or another, except the power to wind up a company in section 81(1)(f) of the Companies Act of 2008. These powers relate to regulation of affected transactions and offers, the power to investigate complaints in respect of those transactions and the power to consult with the Minister respect of those transactions.[36] The Panel may apply for an order to wind up a company in terms section 81(1)(f) where the officers have committed fraud, an illegality or have failed to comply with a compliance notice. The act must have been committed in the previous five years and the officers must have received an administrative fine or a conviction for the same conduct. It appears that this section is aimed at repeat offenders. Presumably, the offences will have to be serious for the Panel to invoke the section. Nevertheless, the section does not give any indications of how and under what circumstances the Panel will exercise this power.

Section 119 sets out the rationales for regulating takeovers and mergers. It provides:

> "119. Panel regulation of affected transactions. — (1) The Panel must regulate any affected transaction or offer in accordance with this Part, Part C and the Takeover Regulations, but without regard to the commercial advantages or disadvantages of any transaction or proposed transaction, in order to—
>
> (a) ensure the integrity of the marketplace and fairness to the holders of the securities of regulated companies;
>
> (b) ensure the provision of—

[35]Section 201 of the Companies Act of 2008 provides that the panel is responsible to ... (a) regulate affected transactions and offers to the extent provided for, and in accordance with, Parts B and C of Chapter 5 and the Takeover Regulations;(*b*) investigate complaints with respect to affected transactions and offers in accordance with Part D of Chapter 7; (c) apply for a court order to wind up a company, in the manner contemplated in section 81 (1) (f); and (d) consult with the Minister in respect of additions, deletions or amendments to the Takeover Regulations.

[36]See Chapter XVA of the Companies Act of 1973.

(i) necessary information to holders of securities of regulated companies, to the extent required to facilitate the making of fair and informed decisions; and

(ii) adequate time for regulated companies and holders of their securities to obtain and provide advice with respect to offers; and

(c) prevent actions by a regulated company designed to impede, frustrate, or defeat an offer, or the making of fair and informed decisions by the holders of that company's securities." [37]

This section encapsulates the general principles previously contained in 11 sections in the SRP Code.[38] These principles have been reduced and subdivided into three subsections.[39] The principles originate from the City Code[40] issued by the UK Panel on Takeovers and Mergers. The policy underlying regulation of takeovers and mergers incorporated in the Takeover Provisions is the same as was applicable to the repealed Companies Act of 1973, and the SRP Code.[41] The General Principles that formed the purpose and the spirit of the SRP Code will still be applicable in regulation of affected transactions.[42] These principles are:

"2. General principles

1. All holders of the same class of securities of an offeree company shall be treated similarly by an offeror.
2. During the course of an offer, or when an offer is in contemplation, neither the offeror nor would be offeror, nor the offeree company, nor any of their respective advisers, shall furnish information to some holders of relevant securities which is not made available to all holders of such securities except with the consent of the Panel.

[37]United Kingdom *The Panel on Takeovers and Mergers The Takeover Code 12th ed* (2016), commonly referred to as the UK City Code Available at http//www.thetakeoverpanel.org.uk/wp-content/uploads/2008/.../code.pdf>(*Acc*essed on 16-4-2017).
[38]Section C of the SRP Code, General Principles of the Code.
[39]Section 119(1) (a), (b) and (c) of the Companies Act of 2008.
[40]See UK City *Code* (2016). See also M Warham "The Takeover Panel" in M Button (ed) *A Practitioners' Guide to the City Code on Takeovers and Mergers. City & Financial Planning* (2006/2007) 2.
[41]P A Delport & Q Vorster *Henochsberg on the Companies Act 71 of 2008* 1 ed (2011) 426(1).
[42]426(2).

3. An offeror shall only announce an offer or its intention to make one after the most careful and responsible consideration. Such an announcement shall be made only when the offeror has proper grounds for believing that it can and will continue to be able to implement the offer. Responsibility in this connection also rests on the financial adviser to the offeror.
4. Holders of relevant securities shall be given sufficient information and advice to enable them to reach a properly informed decision and shall have sufficient time to do so. No relevant information shall be withheld from them.
5. Any document or advertisement addressed to holders of relevant securities containing information or advice from an offeror or the board of the offeree company or their respective advisers shall, as in the case of a prospectus, be prepared with the highest standards of care and accuracy.
6. All parties to an offer shall take all reasonable steps to prevent the creation of a false market in the securities of an offeror or the offeree company. Parties involved in offers shall take care that statements are not made which may mislead holders of relevant securities or the market.
7. After a bona fide offer has been communicated to the board of the offeree company, or after the board of the offeree company has reason to believe that a *bona fide* offer might be imminent, such board may not take any action without the approval of the holders of the relevant securities in general meeting, in relation to the affairs of the company, which could effectively result in any *bona fide* offer being frustrated or in the holders of relevant securities being denied an opportunity to decide on its merits.
8. Rights of control shall be exercised in good faith and the oppression of a minority is unacceptable.
9. The directors of an offeror and the offeree company shall at all times, in advising the holders of relevant securities, act only in their capacity as directors and not have regard to their personal or family shareholdings or to their personal relationships with the companies. It is the interests of holders of relevant securities taken as a whole, which shall be considered when the directors are giving advice to such holders.
10. An affected transaction normally gives rise to an obligation to make a general offer to all other holders of the relevant securities. Where an acquisition is contemplated as a result of which a person may incur such an obligation, he shall, before making the acquisition, ensure that he is

and will continue to be able to implement such an offer.

11. The underlying principle is that persons holding an equity interest in an offeree company through shares or other securities in that company (whether or not such carry voting rights) shall be entitled to dispose of their said interest on terms comparable to those of any affected transaction in the relevant securities."[43]

The Panel must ensure that parties adhere to the provisions of section 119(2), when it regulates takeovers and mergers.[44] Section 119(2) is aimed at ensuring that the objects of section 119(1) are promoted in regulating takeovers and mergers. The provisions aim to achieve the following: that parties undertaking takeovers and mergers do not mislead investors; that there is equality of treatment of shareholders; that no shareholder is preferred above others; that sufficient details about the takeovers or mergers are provided in good time; and that shareholders are not denied an opportunity to decide on the merits of an offer due to insufficient information or information that is provided at a late stage.[45] These requirements emphasise the notion of fairness and equity during a takeover or merger. In order to make an informed decision about a takeover or a merger, shareholders need detailed information that must be provided in good time. By allowing sufficient time, shareholders will have enough time to obtain independent advice should they choose to do so. The City Code[46] also expresses similar principles and these principles form the cornerstone of

[43]Section C of the SRP Code.
[44]Section 119(2) of the Companies Act of 2008 provides that: 'subject to the provisions of subsection (6),
(a) that no person may enter into an affected transaction unless that person is ready, able and willing to implement that transaction;
(b) that all holders of—
(i) any particular class of voting securities of an offeree regulated company are afforded equivalent treatment; and
(ii) voting securities of an offeree regulated company are afforded equitable treatment, having regard to the circumstances;
(c) that no relevant information is withheld from the holders of relevant securities; and
(d) that all holders of relevant securities—
(i) receive the same information from an offeror, potential offeror, or offeree regulated company during the course of an affected transaction, or when an affected transaction is contemplated; and
(ii) are provided sufficient information, and permitted sufficient time, to enable them to reach a properly informed decision.'
[45] Section 119(1) and section 119(2) of the Companies Act of 2008.
[46] See General Principles of the UK City Code.

takeover laws of various jurisdictions, including EU countries and also Australia.[47] The European Directive on Takeovers and Mergers is modeled on the City Code.[48] Accordingly, the principles have also been adopted in the European Directive on Takeovers and Mergers.

The Panel may also require certain disclosures, require filing of documents for approval, issue compliance certificates, receive complaints, and investigate and issue compliance notices in respect of takeovers and mergers.[49] To empower the Panel to carry out its mandate, section 119(5) gives the Panel teeth to ensure compliance. The Panel is able to prohibit and require any action by a person or order a person to divest of an acquired asset, or account for profits.[50] The Panel does not consider the commercial advantages or disadvantages of takeovers and mergers when it regulates such transactions.[51] However, in certain instances the Takeover Provisions provides that the offer must be on the same terms and conditions for all shareholders. In this way the Takeover Provisions may affect the nature and amount of consideration offered for the securities during an affected transaction.[52] In this respect, the Companies Act of 2008 has retained the provisions of the Companies Act of 1973.[53] This is similar to the provisions of the City Code, where the UK Panel does not consider the commercial advantages or disadvantages of takeovers and mergers.[54] It is the domain of shareholders to consider the commercial advantages or disadvantages of takeovers and mergers.[55]

[47]See the EU Takeover Directive. Some of the principles are also applied in Australia. See section 602 of the Australian Corporations Act 2001 dealing with the Eggleston principles, the main principle for regulating takeovers and mergers as discussed in chapter 4 above.
[48]H Baum "Takeover law in the EU and Germany: Comparative analysis of a regulatory model" (2006) *University of Tokyo' Journal of Law and Politics* 360-372.
[49]Section 119(4) of the Companies Act of 2008.
[50]Section 119(5)(b) of the Companies Act of 12008.
[51]Sections 119(1) and 201(3) of the Companies Act of 2008. See also S Luiz "Some Comments on the Scheme of Arrangement as an "Affected Transaction" as defined in the Companies Act 71 of 2008" (2012) PER/PELJ (15) 5.116/638.
[52]See among others; section 123, and 125(2), which requires that parties make a comparable offer in certain circumstances and regulation 111(2), which set a minimum consideration to be offered where, parties have acquired securities for cash during a prescribed period.
[53]Section 440c (2) of the Companies Act of 1973.
[54]Warham "The Takeover Panel" in *A Practitioners' Guide* 1. See also Securities Regulation Code and the Rules of the Securities Regulation Panel (SRP Code). Government Gazette 12962. January of 1991 in the introduction to the SRP Code.
[55]Warham "The Takeover Panel" in A *Practitioners' Guide* 1.

The Takeover Regulations set out the details of the required disclosures and the documents to be filed with the Panel. The Regulations, among other things, provide for when and which document must be submitted, and how such documents must be filed. They also provide for how and when announcements and documents must be sent to shareholders. Further, the Regulations provide that announcements and documents must be approved by the Panel before they are sent to shareholders.[56] The regulations also specifically require companies undertaking transactions to comply with a number of requirements, including providing certain documents to shareholders such as annual financial statements, documents evidencing any valuations of property, memoranda of incorporations or contracts relating to a current takeover or a merger, to be available for inspection by shareholders.[57] It is submitted that practitioners structuring takeovers and mergers, and those drafting offer circulars, can no longer refer only to the regulations as was the case with the SRP Code. Practitioners must refer to both the Takeover Regulations and chapter 5 of the Companies Act of 2008, to determine their obligations and disclosures so as to ensure compliance with the Takeover Provisions.[58] The Companies Act of 1973, in chapter XVA, merely provided a general basis for regulation of takeovers and mergers. Most of the details relating to the underlying principles for regulating takeovers and mergers, including the disclosures, prohibitions and powers of the SRP were in the SRP Code.[59]

[56]Regulation 117 of the Takeover Regulations.
[57]Regulation 106 of the Takeover Regulation requires certain documents to be available for inspection.
[58]See the SRP Code. The SRP Code established rules, which also contained the general principles. The rules among other things created obligations to disclose. The fact that the Act separate obligations and detailed disclosures makes it imperative that both Chapter 5 of the Act and Chapter 5 of the regulations be consulted for undertaking takeovers and mergers, whereas with the SRP Code practitioners could rely on for compliance the regulation in the SRP Code with limited reference to Chapter XVA of the Companies Act of 1973.
[59]Chapter XVA of the Companies Act of 1973 and the SRP Code promulgated in terms of section 440C of the Companies Act of 1973.

5 5 Companies subject to the Takeover Provisions

The Panel regulates affected transactions or offers that involve regulated companies, as defined in the Companies Act of 2008.[60] Regulated companies are defined in paragraph 1 8 of Chapter 1 above. The Takeover Provisions mainly affect public companies due to their widely-held shareholding. The requirements to comply with the Companies Act of 2008 for public companies is similar to that of the Companies Act of 1973 and the SRP Code. This also applies to state-owned companies.[61]

However, there is a significant difference between the requirement of the Companies Act of 2008 and that of the Companies Act of 1973 in respect of the regulation of takeovers and mergers of private companies. The SRP Code only applied to private companies where it had more than 10 beneficial shareholders and the transaction value was more than R5 million. In addition, the provisions were only included in the SRP Code - a regulation - whereas in terms of the Companies Act of 2008, the provisions are in the Companies Act of 2008 and the Takeover Regulations.[62] There is no provision for a general exemption from compliance for private companies. Once a company is defined as a regulated company,[63] it must comply with the takeover provisions whenever it undertakes an affected transaction or it must specifically apply to the Panel for exemption.

However, the Companies Act of 2008 provides for voluntary compliance in section 118(1)(c)(ii) by private companies that are not defined as regulated companies. This provision may protect the interests of minority shareholders better as it provides for enforcement of takeover provisions by the Panel during takeovers and mergers by private companies that have adopted voluntary compliance. The definition of private companies that are regulated companies, requires 10 percent share dealings in a period of 24 months. It has been criticised harshly by a number of researchers. The section unnecessarily

[60]See section 117 dealing with definitions and section 118 dealing with companies that are subject to the Takeover Provisions under the Companies Act of 2008.
[61]Chapter XVA of the Companies Act of 1973 read with section A3 of the SRP Code.
[62]Section A3 of the SRP Code.
[63]See definition of regulated company in chapter 1, paragraph 1 of the dissertation.

burdens small private companies with compliance and associated costs. These companies will be forced to comply with takeover and merger provisions or have to apply for an exemption to the Panel. It is submitted that this is another addition of bureaucratic compliance and resultant costs for small businesses. The threshold of 10 percent required by section 118(2) of the Companies Act of 2008 has been criticised for being an irrelevant criterion.[64] The logical and commercial measure to determine the type of companies that should be subject to the Takeover Provisions should be value and the number of shareholders.[65]

The section goes against the objectives of the Companies Act of 2008 in section 7, as discussed in paragraph 5 2 above.[66] One of the objectives is to reduce costs for small companies. Criticism is also expressed by other practitioners who indicate that the benefits of transparency, as weighed against the costs of compliance, are disproportionate and, at worst, unnecessary.[67] There are problems relating to the applicability of the Takeover Provisions to private companies.[68] It is suggested that the 24 months trading period and 10 percent transfer of shares test in private companies has unintended consequences in that even very small companies, or companies that have not yet traded, will be forced to comply with the requirements of the takeover provisions. This requirement for regulated companies is much broader than is necessary. By casting the net so wide, it appears that the legislature assumed that the majority of private company shareholders require the protective measures in the takeover provisions.

The Companies Act of 2008 does not even seem to consider that, in certain circumstances, shareholders may have developed their own protective measures in their constitutions, and therefore do not need special protection in

[64] HE Wainer "The new Companies Act: Peculiarities and Anomalies" (2010) 126 (part 4) *South African Law Journal* 825.
[65] Wainer (2010) *South African Law Journal* 825.
[66] See also Wainer (2010) *South African Law Journal* 825 referring to the objectives of the Companies Bill, where it is indicated that the Act should reduce costs of doing business for small companies.
[67] N Boardman "A critical analysis of the new South African takeover laws as proposed under the Companies Act 71 of 2008" (2010) *Acta Juridica* 318.
[68] PJ Sutherland "The state of Company Law in South Africa: A review of modern company law for a competitive SA Economy by T Mongalo (ed)" (2012) 1 *Stell LR* 157.

terms of the Act. It is pointed out that, although companies may be entitled to apply for exemptions from the Panel in terms of section 119(6) of the Companies Act of 2008, such applications come at a cost. Companies may need to seek advisers and pay filing fees in order to obtain such exemptions. It is also not appropriate to achieve regulation by exemption, and this may affect the efficiency of the regulatory measures and introduce an additional burden on both the regulators and the parties who are required to comply with the regulations. Applications for exemptions create complexity and unnecessary formalism.[69]

The Panel regulates affected transactions undertaken by private companies in a flexible manner, as contemplated by the DTI 2004 Policy document and section 7.[70] The Panel does not enforce a strict formalistic approach to compliance in respect of affected transactions by small, regulated private companies. The Panel has introduced guidelines to deal with regulation of affected transactions by small regulated private companies.[71] The practice ensures that affected transactions do not have to comply with the full disclosures required by parts B and C in Chapter 5 of the Act. The guidelines allow private regulated companies to submit applications for exemption from compliance with the Takeover Provisions in accordance with section 119(6) of the Act. Evidence suggests that the majority of exemptions granted by the Panel relate to affected transactions by private regulated companies.[72]

It is suggested that the basis for regulating takeovers and mergers by private companies set out in the SRP Code should have been retained, but with a higher threshold in number of shareholders and the value of transactions. This would allow oversight by regulators and simultaneously ensure that any possible prejudice to minority shareholders in private companies is limited. At

[69]Sutherland (2012) *Stell LR* 174.
[70]See the discussions in paragraph 5 2 dealing with the objectives of the Companies Act of 2008.
[71]See Guideline 3/2011. Available of http//trpanel.co.za. Accessed 2 .2.2019.
[72]See Annexure 1 to the *Takeover Regulation Panel Annual Report* for the 13 months ended 31 March 2013. 39.

the same time, it will avoid the unintended consequences of adding a burden of compliance and costs to small private companies.

5 6 Types of affected transactions regulated

5 6 1 Introduction

Section 117(1)(c) of the Companies Act of 2008, lists seven affected transactions relating to regulated companies.[73] These transactions, are in common parlance, takeovers or mergers of companies.[74] While the focus of the dissertation is the mandatory offer, it is also important to provide an overview of other methods of achieving takeovers and mergers. These other affected transactions are discussed to provide a broad overview of the different types of takeover methods and show how their enforcement offers alternative protection to minority shareholders during such takeovers or mergers. Accordingly, the discussions of these affected transactions are not exhaustive.

5 6 2 Section 112: Proposals to dispose of all or the greater part of assets or undertaking of a company

Section 112 of the Companies Act of 2008 deals with the disposal of all or the greater parts of the assets or undertaking of a company. Like the Companies Act of 1973, the Companies Act of 2008 does not define what 'dispose' means in this context.[75] It is submitted that some of the definitions provided will influence how the section is interpreted. Given the similarities between the Companies Act of 1973 and the Companies Act of 2008, guidance may be sought from previous judicial decisions as to what is meant by 'dispose.'[76] To dispose means 'to part with' or 'to get rid of' and contemplates permanently depriving the company of any rights to the ownership of the assets.[77] The courts

[73]See also Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 426(5).
[74]See definitions in paragraph 1 8 above.
[75]JL Yeats, RA de la Harpe, RD Jooste, H Stoop, R Cassim, J Seligmann, L Kent, RS Bradstreet, RC Williams, MF Cassim, E Swanepoel, FHI Cassim and KA Jarvis *Commentary on the Companies Act of 2008* (2018) 5-3.
[76]Yeats et al *Commentary on the Companies Act of 2008* 5-3.
[77]5-3.

have given direction as to what may constitute a disposal. The question whether cessions and pledges are disposals, in particular, has been addressed. A cession or pledging of shares *in securitatem debiti (*and not an out and out cession), is not a disposal of the shares provided that the reversionary rights are preserved. This is so because during the period when the shares are ceded, the cessionary is not free to dispose of those shares, but has an obligation to cede the rights back to the cedent once the debt has been paid.[78] The passing of a mortgage bond over a company's assets has also been clarified. In the matter of *Standard Bank of South Africa Limited v Hunkydory Investments 188 (Pty) Limited,*[79] the court ruled that the passing of a mortgage bond over immovable property is not a disposal of assets as contemplated in terms of section 228 of the Companies Act of 1973.[80] The court clarified that to dispose in that section meant the act of transferring ownership. A transaction in terms of which a debtor agrees to hypothecate his property, is not a disposal to the creditor or anyone. Such an interpretation would extend the meaning of the section beyond what was intended by the legislation.[81] The legislature referred to disposal in the ordinary and narrower sense.[82] The section is aimed at those disposals that transfer ownership of the assets and not a transaction that exposes the company's assets to the risk of a forced disposal of those assets because of the borrowing.[83] It is inaccurate to characterise a mortgage bond as one of the steps to a sale in execution and therefore a disposal, because in the event of the execution, it is the sheriff who enforces or executes the forced sale of the property.[84] The correct view is that a disposal has occurred when there is an unconditional, binding agreement to dispose the assets. Where the disposal is subject to a condition, it is impossible to say, before the condition is fulfilled, whether or not the entering into the contract disposed of the property. When the condition is fulfilled, the making of the contract had the effect of the

[78]5-3.
[79]Case No 15427 /2008(WCC).
[80] Case No 15427 /2008(WCC) par 23
[81]Case No 15427 /2008(WCC) 23 and Yeats et al *Commentary on the Companies Act of 2008* 5-4.
[82]Yeats et al *Commentary on the Companies Act of 2008* 5-4.
[83]5-4.
[84]J Latsky "The fundamental transactions under the Companies Act: A report back from practice after the first few years" (2014) 2 *Stell LR* 366.

disposal of the property and if the condition is not fulfilled, the making of the contract had no legal effect at all.[85]

A disposal of the assets or undertaking is one of the methods of taking over or merging a company's operations. The method can be used to obtain control over the business of a company without purchasing the shares of the company, "and is one of the ways for a predator to takeover a business."[86] Disposals of all or greater parts of the assets or undertaking of a company were not regarded as affected transactions until the amendment of the Companies Act of 1973 by the Corporate Laws Amendment Act No.24 of 2006 that became effective 14 December 2007. The effect of section 112 is substantially similar to section 228 of the Companies Act of 1973.

However, the wording of section 112 is significantly different in that the Companies Act of 1973 referred to the capacity of director, while the Companies Act of 2008 refers to the capacity of the company.[87] The new section includes a definition of all or the greater part of the assets or undertaking being disposed of, as opposed to the Companies Act of 1973 that did not provide such a definition.[88] Section 228 of the Companies Act of 1973 was deficient in this respect. Another useful addition to the 'disposal of assets' section is the requirement that the fair value of assets disposed must be disclosed. Section 112(4) states that any part of the undertaking or assets of a company to be disposed of, as contemplated in this section, must be fairly valued, as calculated in the 'prescribed manner', as at the date of the proposal, which date must be determined in the 'prescribed manner'. The regulations do not indicate what is the 'prescribed manner' by which the assets or undertaking must be valued. It is asserted that the regulations need to be amended to avoid uncertainty.[89] Where a disposal relates to a regulated company, sections

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[85]366.
[86]363.
[87]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 404.
[88]Section 1 of the Companies Act of 2008 of the Act defines "All or the greater part of the assets or undertaking" as meaning more than 50 percent of the company's gross assets at fair market value, irrespective of its liabilities; or more than 50 percent of the company's value of its entire undertaking, at fair market value.
[89]Latsky (2014) *Stell LR* 364.

114(2) and (3), read with regulation 90, will apply. Regulation 90 requires parties to obtain a ruling from the Panel and, if the Panel rules that an expert opinion is required, the parties must proceed to obtain such an opinion in terms of regulation 90. The regulation creates an obligation to retain an independent expert to advise the company in respect of a section 112 transaction instead of the section creating such an obligation. The regulation prescribes that the valuation must be done in accordance with generally- accepted valuation approaches and methods in use from time to time. The methods include the: (a) capitalisation, income or cash flow approach which relies on the 'value–in–use' principle and requires determination of the present value of future cash flows over the useful life of the asset or the business; (b) comparative or market approach that relies on the principle of the 'willing buyer, willing seller' and requires that the amount obtainable from the sale of an asset or undertaking is determined as if in an arm's length transaction; and (c) cost approach that relies on historical amounts spent on asset or undertaking.[90]

It would have been preferable if the obligation was in the section itself, rather than in the regulation, as this is not the right place to create an obligation and may be *ultra vires* as it is created in a subordinate legislation.[91] The disposal must be considered independently of any other disposals. Accordingly, it is not aimed at seeking shareholders' approval for a number of disposals that collectively would qualify as a disposal of all or the greater part of the assets or undertaking of a company.[92] Section 112(5) also provides that the authorisation must only be granted for specific transactions. The authorisation required must be by special resolution. Prior to its amendment, the Companies Act of 1973 allowed disposals by ordinary resolution.[93] Section 112 does not have a specific reference to ratification, unlike section 228 of the Companies Act of 1973. The Companies Amendment Act 3 of 2011 removed reference to ratification that was in section 115(5) of the Act. Delport and Vorster indicate that ratification of

[90]Regulation 90(4).
[91]See regulation 90 that creates the obligation. This is different to the obligation created by section 114(2) of the Companies Ac of 2008 in respect of schemes of arrangement.
[92]Delport *Henochsberg on the Companies Act* 408(1).
[93]See Corporate Laws Amendment Act No.24 of 2006.

a contract already concluded by the company, will be sufficient.[94] However, there is a view that, unlike section 228 of the Companies Act of 1973, the Companies Act of 2008 does not allow ratification of a disposal.[95] It appears that the matter is not clear as the common law generally allows ratification where authorization is required. It can be argued that the deletion of ratification does not exclude ratification in common law. The deletion of "ratifies" by the legislature makes it unclear as to whether the common-law position applies.[96] A question has been asked as to whether shareholder approval relates to the conclusion of the agreement of disposal or to the implementation of the agreement. Is the agreement binding without shareholder approval? This issue created difficulty in the Companies Act of 1973 and it remains unclear and uncertain.[97]

There is support for a view that a disposal transaction that does not comply with the requirements of the Companies Act of 2008 is not void, but is unenforceable as between the parties.[98] It has been suggested that it is important to know when a disposal has taken place. Once a disposal has happened it may be too late to comply with the Act.[99] It is a moot point among practitioners whether a disposal in terms of section 112 can be approved by means of a written resolution, in terms of section 60. The preferred view is that there must be a meeting of shareholders complying with the requirements of section 115. It cannot be done by means of a 'round robin' resolution.[100] Section 115(2) (a), which indicates that the transaction must be approved by "a special resolution adopted… at a meeting called for that purpose," seems to support the assertion.[101] A disposal in terms of section 112 entitles shareholders of the company to exercise appraisal rights in terms of section 164. Should a disposal

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[94]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 404.
[95]Latsky (2014) *Stell LR* 365.
[96]365.
[97]CM Cassim & J Yeats "Fundamental Transactions, Takeovers and Offers" in FHI Cassim (Man Ed) (2012) *Contemporary Company Law* 720.
[98]Latsky (2014) Stell *LR* 367 and also Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 404, who state that an agreement that has not been approved as required is not void or invalid but cannot be enforced.
[99]Latsky (2014) *Stell LR* 365.
[100]363.
[101]363.

be approved in terms of a round-robin resolution, exercising appraisal rights can prove to be unworkable due to numerous procedural steps that shareholders must undertake to exercise the appraisal rights. Nevertheless, the validity and enforceability of a disposal that does not comply with the Act has not yet been clearly determined by the courts. This uncertainty will exist until clarified by the courts.[102] The novelty of the issues raised by application of section 112 leads to a number of unanswered questions that requires further research. Further, the dearth of research on this topic limits the discussions. The development of case law will assist in the interpretation of the section.

In *Moraitis Investments (Pty) v Montic Dairy*,[103] the Supreme Court of Appeal had to consider the principle of unanimous assent for the purposes of approval of a section 112 disposal.[104] Before applying the principle, the court pointed out that the principle has long been recognised as part of English company law, that has been accepted as part of South African company law.[105] The appellant in this matter argued that a transaction contemplated in a settlement agreement entered into earlier by the parties, was subject to the requirements of sections 112 and 115 and, therefore, could only be implemented in terms of a special resolution. The court disagreed with the contention.[106] The court pointed out that the purpose underpinning the requirements of sections 112 and 115 is to ensure that the interests and views of all shareholders are taken into account before a company disposes of the whole or the greater part of its assets or its undertaking.[107] Sections 65(9) and (10) of the Companies Act of 2008, stipulate the majority required for the passing of a special resolution, which is 75 percent of the voting rights exercised on the resolution or such percentage as may be allowed by the company's MOI. The court held that, where the company has a single shareholder, these requirements are a mere formality.[108] The court extended the application of the principle of unanimous assent to special

[102]Latsky (2014) *Stell* 363.
[103]Case no: 799/2016 (SCA).
[104]Case No 799/2016 para 37.
[105]Case No 799/2016 para 37.
[106]Case No 799/2016 para 40.
[107]Case No 799/2016 para 37.
[108]Case No 799/2016 para 37

resolutions.[109] The burden of proving unanimous consent where multiple shareholders are involved may be too onerous to discharge. Therefore, it is prudent to ensure that all special resolutions are passed in accordance with the required formalities.[110] This is even more so where filing at the CIPC is required.[111]

5 6 3 Section 113 – Proposals for amalgamations or mergers

The second type of an affected transaction is an amalgamation or a merger transaction.[112] This is a new type of transaction, which has been introduced in section 113 of the Companies Act of 2008. The transaction requires a consensual process between the various companies involved in the transaction.[113] According to the DTI 2004 Policy document, this new type of transaction is aimed at introducing efficient takeovers and mergers.[114] The amalgamation or merger in terms of section 113 is a new fundamental and radical concept borrowed from the US.[115] However, it is submitted that such an introduction is to be welcomed. It makes takeovers or mergers simple and efficient and contributes to the facilitation of mergers and takeovers.[116]

[109] C Wood and S Singh "The doctrine of unanimous assent" (2018) *Without Prejudice* 8.
[110] 8.
[111] 8.
[112] Section 1 of the Companies Act of 2008 defines amalgamations or mergers as meaning a transaction, or series of transactions, pursuant to an agreement between two or more companies, resulting in—
(*a*) the formation of one or more new companies, which together hold all of the assets and liabilities that were held by any of the amalgamating or merging companies immediately before the implementation of the agreement, and the dissolution of each of the amalgamating or merging companies; or
(*b*) the survival of at least one of the amalgamating or merging companies, with or without the formation of one or more new companies, and the vesting in the surviving company or companies, together with such new company or companies, of all of the assets and liabilities that were held by any of the amalgamating or merging companies immediately before the implementation of the agreement.
[113] Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 408.
[114] DTI 2004 Policy document 43.
[115] Cassim & Yeats "Fundamental Transactions, Takeovers and Offers" in *Contemporary Company Law* 676.
[116] 677.

The new amalgamations and mergers provisions in section 113, read with section 116, of the Companies Act of 2008 are innovative.[117] South Africa has never had a statutory merger in the true sense.[118] The amalgamations or merger provisions have been transplanted from the US but have been adapted to suit local company law. Davids *et al*[119] deal with these transactions in detail and convincingly indicate the merits of these types of transactions. They point out that the new provisions will facilitate the creation of business combinations, as several companies may merge their operations in terms of the section. Cassim, in a comprehensive analysis of this section, indicates that the introduction of the section is a significant liberalisation of policy by the legislature.[120]

Section 113 is useful for intragroup mergers. One company may absorb the operations of another or others without approaching each individual party to contract with.[121] There is no formal distinction between an amalgamation and a merger.[122] The only distinction between the two transactions seems to be that, in an amalgamation, a new company is formed while, in the case of a merger, existing companies are involved in the transaction.[123] The merger or amalgamation procedure in terms of the Companies Act of 2008 is a simple procedure which requires a number of steps to be completed: An agreement needs to be signed by the companies, shareholders of the companies have to cast a vote based on disclosures, and dissenting shareholders are afforded an appraisal right to have the shares bought at 'fair value' in terms of section 164 of the Act. The courts only play a role in specified circumstances.[124]

Section 116 of the Companies Act of 2008 dealing with the implementation of an amalgamation or merger also provides additional requirements for

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[117]Sutherland (2012) *Stell LR* 1.
[118]CM Cassim "The Introduction of Statutory Mergers in South African Corporate Law: Majority Rule Offset by the Appraisal Right (Part 1)" (2008) *SA Merc LJ* 1–32, 1.
[119]Davids *et al* (2010) *Acta Juridica* 337-338.
[120]Cassim (2008) *SA Merc LJ* 1–32, 1.
[121]Latsky (2014) *Stell LR* 377.
[122]Davids *et al* (2010) *Acta Juridica* 337-338. 341.
[123]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 408.
[124]Cassim & Yeats "Fundamental Transactions, Takeovers and Offers" in *Contemporary Company Law* 618.

completion of a merger or amalgamation that are intended to protect creditors. The provisions include: (a) filing of a notice of the merger in the prescribed manner by the merging companies to all known creditors;(b) protection of creditors in that, on receipt of notice, they may apply to court to review the merger on the basis they may be materially prejudiced. However, the court may grant leave to apply for review of the merger only if: it is satisfied that the applicant is acting in good faith, the merger, if implemented, would materially prejudice the creditor and there are no other remedies available to the creditor.[125]

Further requirements for the notice of a merger include: filing with the Companies Commission and confirmation that the transaction has satisfied the requirements of section 115 relating to voting.[126] The notice must also include confirmations that approvals or consents have been obtained from other regulators if so required, such as in terms of the Competition Act or the financial services legislation. Any other shareholder approvals that are still required, such as, for the amendment of the Memorandum of Incorporation of any newly-incorporated company must be disclosed.[127] On receipt of the notice of the merger agreement, the Companies Commissioner must complete a number of administrative steps. These include: issuing new registration certificates for new companies and deregistering any of the merged companies that did not survive the merger.[128]

The effect of the merger agreement is that implementation is subject to conditions set in the merger agreement; any existing liabilities are not affected; any pending or existing civil, criminal or administrative actions or proceedings may continue against or in favour of any merged company. Any order, ruling, judgment or conviction against or in favour of any merged company is also not affected by such merger agreement.[129] Section 116(7) deals with the impact of

[125]See section 116(1) of the Companies Act of 2008.
[126]The requirements of section 115 of the Companies Act of 2008 are discussed separately under paragraph 5 6 6 below.
[127]See section 116(3) and section116(4) of the Companies Act of 2008.
[128]See section 116(5) of the Companies Act of 2008.
[129]Section 116(6) of the Companies Act of 2008.

the merger agreement on property rights of each merged or surviving company. The property of each merging company becomes the property of the newly-merged or surviving company. The newly-merged or surviving company is also liable for the obligations of the merging company. The above rights and obligations are in accordance with the terms and conditions of the merger agreement but are subject to the requirement that each merged company must meet the liquidity and solvency tests. Where a property registered in terms of public regulation is required to be transferred from one merging company to another in terms of the merger agreement, the registrar of deeds may effect registration of such property on production of the copy of the merger agreement and the filed notice of merger agreement. The provisions of the Banks Act 94 of 1990, prevail over those of section 116(7) in case of a conflict between them.[130]

The legislature is trying to balance the interests of the shareholders and economic growth by introducing the statutory merger to facilitate such transactions.[131] However, there is lack of clarity in this section due to the fact that there is no definition of what an amalgamation or merger is.[132] It is also not easy to determine which transactions may be undertaken using which mechanism.[133] It is further asserted that the legal effect on the transfer of assets and liabilities following the completion of an amalgamation or merger in terms of section 113 is not clear.[134] It, for instance, is not clear what their effect will be on existing contractual rights. A question has been raised regarding the impact of a merger on pre-emptive rights where the shareholder is a company. Can failure to offer the shares to other shareholders be regarded as a breach of a clause in the MOI that grants a pre-emption right to those shareholders? This question is controversial and uncertain in those jurisdictions where the section originated.[135] The requirements of sections 113 are not clear or specific on the issue. It is generally accepted that statutory mergers should be

[130]See section 116(9) of the Companies Act of 2008.
[131]Cassim (2008) *SA Merc LJ* 1–32 1.
[132]Sutherland 2012 *Stell LR* 175.
[133]175.
[134]175.
[135]Latsky (2014) *Stell LR* 375.

welcomed. However, it is also asserted that the relevant sections need to be tidied to remove uncertainties.[136]

5 6 4 Section 114 – Proposals for schemes of arrangement

Schemes of arrangement in terms of section 114(1) are defined as the third type of affected transaction in section 117(1)(c). The scheme of arrangement procedure in terms of the Companies Act of 2008 is fundamentally different, and in significant respects, from the previous procedure for schemes of arrangement in terms of section 311 of the Companies Act of 1973. The Companies Act of 2008 specifically refers to a number of transactions that will constitute arrangements by the company including, divisions, consolidations, expropriations, exchange and repurchases of securities. It is submitted that providing specific instances where the scheme of arrangement may be used, suggests that the legislature intends to facilitate these schemes.[137] Not all schemes of arrangements qualify as affected transactions subject to the Takeover Provisions because they might not involve a regulated company. Such a scheme would be regulated as a fundamental transaction only.[138]

The requirements for a scheme of arrangement in terms of section 114 are simple and clear. Although the expression "scheme of arrangement" is not defined, it appears that "just about any arrangement between the company and holders of a class of securities would qualify as a scheme if the company has complied with the requirements of the Act."[139] There is no *numerus clausus* of transactions with shareholders and the company that could qualify as schemes of arrangement.[140] The "arrangements" contemplated by this section:

> "[A]re of the widest character and … the only limitations are that the scheme cannot authorise something contrary to the general law or wholly *ultra vires* the

[136]See Sutherland (2012) *Stell LR* 175.
[137]Cassim & Yeats "Fundamental Transactions, Takeovers and Offers" in *Contemporary Company Law* 659.
[138]Luiz (2014) *Merc LJ* 573 at note 83.
[139]Latsky (2014) *Stell LR* 369.
[140]369.

company …' and that if capital is to be reduced the formalities [as prescribed by ss 83 *et seq* in terms of the 1973 Act] 'must also be complied with'".[141]

The principle applied in *Ex parte Federale Nywerhede Bpk,*[142] that there is no reason to give a narrow or limited meaning to an arrangement, has been maintained in section 114. The section is now specific and it is clear that any number of arrangements may be entered into using the section. There are safeguards for shareholders in the scheme of arrangement in terms of section 114. These are in the form of disclosures required by the Act, including the independent expert report, a requirement that there must be a quorum of 25 percent of the shareholders entitled to vote, and the transaction must be approved by 75 percent of those entitled to vote in terms of section 115(2)(a). The special resolution must be passed by independent votes.[143] Shareholders may unanimously waive the requirement for independent expert advice in section 114. This is in line with the general principle that a beneficiary of a right may freely waive such a right if such a waiver does not raise any public interest concerns.[144] The requirement for the expert report is required for the benefit of shareholders as a whole. Where a scheme of arrangement is used to effect a merger those who sell may be prejudiced if the shares are sold at a low price, and those who remain may also be prejudiced if the shares are bought at a high price. A waiver of the expert report by well-informed directors and shareholders should not present a high risk to directors. However, there is nevertheless a risk and directors should not lightly agree to such a waiver.[145]

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[141]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 410.
[142]1975 (1) SA 826 W 830. In this case the court quoted from the English case *Re National Bank Ltd*.,(1966) 1 All E.R 1006, that rejected a limitation or qualification on the generality of the word 'arrangement' in section 206 of the UK Companies Act of 1948.In that case, the court indicated that the legislature had not seen fit to impose a limitation and the court did not see any reason for implying any.
[143]See section 115(4) of the Companies Act of 2008 which provides that (4) For the purposes of subsections (2) and (3), any voting rights controlled by an acquiring party, a person related to an acquiring party, or a person acting in concert with either of them, must not be included in calculating the percentage of voting rights—
(*a*) required to be present, or actually present, in determining whether the applicable quorum requirements are satisfied; or
(*b*) required to be voted in support of a resolution, or actually voted in support of the resolution. See also S Luiz "Case Comments: Use of a Schemes of arrangement to Eliminate Minority Shareholders" (2010) *22 SA Merc LJ* 449.
[144]Latsky (2014) *Stell LR* 370.
[145]371.

A brief excursion into the UK Companies Act 2006 on the subject of schemes of arrangement is appropriate in order to put the South African scheme of arrangement in perspective. The courts in the UK have rejected an argument that where a scheme is used as an alternative to a takeover offer, the threshold for voting should be 90 percent rather than 75 percent.[146] The UK Companies Act 2006 does not prescribe the subject matter of schemes of arrangement. A scheme of arrangement could also include a compromise or arrangement between a company and its creditors.[147]

Schemes of arrangement, rather than the traditional takeover offer have been a preferred takeover method of choice in the UK for a number of years.[148] The scheme of arrangement requires approval of 75 percent of qualifying offeree company shareholders to proceed. In a scheme of arrangement, the offeror deals with the board of directors of the offeree company. Often a transaction agreement is entered into between the board of the offeree company and the offeror, in terms of which each party undertakes to ensure that certain steps are undertaken. The scheme is a corporate action of the offeree company and is therefore controlled by the offeree board. The directors of the offeree must agree and recommend proposing a scheme of arrangement to the shareholders. The offeree company directors must include a special resolution as part of the scheme document so that shareholders can vote to have their shares expropriated and pass control to the offeror.

A friendly relationship with the offeree company board is therefore a pre-requisite to propose a scheme of arrangement between the offeree and its shareholders. In contrast to a takeover offer, there can be no hostile scheme of arrangement.[149] Protection of minority shareholders in a company where a scheme of arrangement is proposed consists of the requirement that the

[146]J Payne "Schemes of Arrangement, Takeovers and Minority Shareholder Protection" (2011) II Part 1 *Journal of Corporate Law Studies* 72.
[147]See Payne (2011) *Journal of Corporate Law Studies* 88.
[148]See N Boardman "Public Takeover Offer Versus Schemes of Arrangement" *Corporate* (March 2012). Boardman is one of the drafters of the Companies Act 2008.
[149]Payne (2011) *JCLS* 70.

scheme must be approved by a special resolution adopted by persons entitled to exercise voting rights on such matter, at a meeting called for that purpose and at which sufficient persons are present to exercise, in aggregate, at least 25 percent of all the voting rights that are entitled to be exercised on that matter, or any higher percentage as may be required by the company's Memorandum of Incorporation.[150] It is notable that the section specifically indicates that the approval may be by a higher threshold.[151] It is suggested that directors may not lower the threshold for approvals of fundamental transactions, but may set a higher threshold, if the Memorandum of Incorporation of the company allows this.[152] Arguably, the higher the threshold for approval, the more protection offered to shareholders during a fundamental transaction. In the UK, a scheme of arrangement requires court approval. Once all the formalities have been complied with, it is likely that the court will approve the scheme.[153]

In SA, section 311 of the Companies Act of 1973 also required the court to approve the scheme. But the Companies Act of 2008 simplified this procedure. In terms of section 114, only shareholder approval is required and court involvement will only apply in certain circumstances.[154] Court involvement is, therefore, no longer mandatory. This is in line with the DTI 2004 Policy document to avoid excessive formalism and the need to improve efficiency in regulation of takeovers and mergers.[155]

The legislature seeks to ensure that companies can obtain shareholder approval in an efficient manner. The removal of automatic court involvement does not mean that shareholders have been left unprotected, as shareholders can still approach the courts in terms of section 115(3), provided that certain

[150]Section115(2)(a) of the Companies Act 2008.
[151]Section 115(2) (a).
[152]In terms of section 64(2 of the Companies Act, a company may provide in its Memorandum of Incorporation a lower quorum for meeting than 25 percent but this is not allowed for the purposes of approving a fundamental transaction
[153]Boardman (2010) *Act Juridica* 316.
[154]Section 115 of the Act provides for court intervention where certain requirements have been met, such as where 15 percent of holders voted against the relevant resolution and sought court approval, or where the company applies to court for such approval.
[155]See Boardman (2010) *Act Juridica* 315.

requirements are met.[156] In terms of the section, a company may not proceed to implement a resolution to implement a scheme without the approval of a court if-

> "(a) the resolution was opposed by at least 15 percent of the voting rights that were exercised on that resolution and, within five business days after the vote, any person who voted against the resolution requires the company to seek court approval; or
> (b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave, in terms of subsection (6), to apply to a court for a review of the transaction in accordance with subsection (7)."[157]

The court may grant relief to the shareholders and set aside the resolution to approve the scheme where:

> "(a) the resolution is manifestly unfair to any class of holders of the company's securities; or
> (b) the vote was materially tainted by conflict of interest, inadequate disclosure, failure to comply with the Act, the Memorandum of Incorporation or any applicable rules of the company, or other significant and material procedural irregularity."[158]

The additional protection for shareholders is the appraisals right in terms of section 164. This right is discussed below in paragraph 5 6 6. It appears that the legislature has achieved a balancing of interests for the parties involved in schemes of arrangements by introducing simplicity, efficiency and additional protection for shareholders.

[156] Section 115 of the Companies Act of 2008.
[157] Section 115(3) of the Companies Act of 2008.
[158] Section 115 (7) of the Companies Act 71 of 2008.

5 6 5 *Section 48(8) (b) – Share repurchases*

In this paragraph, share repurchases are discussed only in so far as they are affected transactions and, accordingly, this part has a limited scope. The Companies Amendment Act of 2011, introduced share repurchases in section 48(8)(b) into the Companies Act of 2008. The Companies Act of 1973, prior to its amendment, did not allow for general share repurchases mainly due to capital maintenance rules for the protection of creditors and shareholders.[159] An amendment to the Companies Act of 1973 introduced sections 85-90, which dealt with acquisition of shares. The sections provided for repurchase of shares subject to safeguards for creditors and shareholders.[160] The articles of the company had to make provision for share repurchases before the company could proceed with a share repurchase.[161] In addition, the company had to pass a special resolution. The resolution could authorise a specific or general share repurchase. A general resolution was only effective until the next general meeting of the company.[162] Further, in doing a buy-back, the directors of the company had to comply with liquidity and solvency requirements.[163] A company could not repurchase all its shares to the point where it no longer had issued shares.[164]

The Companies Act of 2008 also allows for repurchase of shares subject to certain requirements including: (a) directors' resolutions; (b) solvency and liquidity requirements under section 46 and; (c) compliance with sections 114 and 115, as detailed underneath. It also attempts to ensure that all shares in the company will not be repurchased to the point where it will no longer have shares apart from shares held by a subsidiary or shares that are convertible or redeemable.[165] However, there are clear differences between the Companies Act of 1973 and the Companies Act of 2008 on how share repurchases must be regulated. Section 48 of the Companies Act of 2008 emphasises that the

[159]R Jooste "Corporate Finance" in FHI Cassim (Man Ed) *Contemporary Company Law* 294.
[160]See the Companies Amendment Act 37 of 1999.
[161]See section 85(1) of the Companies Act of 1973.
[162]See section 85(2) of the Companies of 1973.
[163]Section 85(4) of the Companies Act of 1973.
[164]See section 85(9) of the Companies Act of 1973.
[165]Section 48(3) of the Companies Act of 2008.

responsibility for repurchasing shares rests with the board. It must authorize a repurchase and such a repurchase must comply with the requirements for a distribution in section 46, which includes that it must reasonably appear that the company will afterwards remain solvent and liquid, and that the board must acknowledge that they have applied the solvency and liquidity test and that they have reasonably concluded that this test will be met.[166] More importantly, section 48(8) does not distinguish between selective and general share repurchases and it does not generally require shareholders to approve these transactions. Furthermore, it was felt that this did not provide adequate protection to shareholders and section 48(8) was added by the Amendment Act 3 of 2011. Approval by special resolution is now required for repurchases from directors, prescribed officers or parties related to them. Moreover, and most significant for this thesis, share repurchase of 5 percent or more of the shares of a company was made subject to the requirements of sections 114 and 115 of the Act.[167] Section 48(8) raises a number of debates as discussed underneath.

The section appears to introduce another "affected transaction" or a "fundamental transaction" through a 'back door'.[168] The section seems to impose the requirements of affected transactions and fundamental transactions by subjecting share repurchases in terms of section 48(8)(b) to the requirements of sections 114 and 115 of the Companies Act of 2008. A section 114 scheme of arrangement is listed under part A of chapter 5 as a fundamental transaction and section 115 deals with procedural requirements to approve fundamental transactions. It has been argued by some practitioners that all

[166]Section 46(1) of the Companies Act of 2008.
[167]See section 48(8)(b) of the Companies Act of 2008.
[168]Section 48 of the Companies Act of 2008 (relating to share repurchase of shares) provides that: '(8) A decision by the board of a company contemplated in subsection (2) (a (i.e. to repurchase the shares)—(a) must be approved by a special resolution of the shareholders of the company if any shares are to be acquired by the company from a director or prescribed officer of the company, or a person related to a director or prescribed officer of the company; and
(b) is subject to the requirements of sections 114 and 115 if, considered alone, or together with other transactions in an integrated series of transactions, it involves the acquisition by the company of more than 5 percent of the issued shares of any particular class of the company's shares.'

share repurchases for more than five percent of the issued shares of a company must be undertaken in terms of a scheme of arrangement and section 115 of the Companies Act of 2008. Conversely, it has been asserted that share repurchases in terms of this section merely require parties to comply with the procedural requirements of section 115. According to this approach a repurchase does not become a scheme of arrangement.[169] The section is not clear in this regard.[170] It is pointed out that the reference to “subject to the requirements of sections 114 and 115” does not imply that the repurchase is a scheme of arrangement. Should that have been the intention of the legislature, the section would not have emphasised “the requirements.”[171] Furthermore, common law rules provide that where a mandatory procedure has been prescribed in the Act, that procedure cannot be substituted by a scheme of arrangement.[172] It is also pointed out that:

> “Section 48(8) of the Companies Act provides merely that a reacquisition of securities contemplated that section “is subject to the requirements of section 114. It does not provide that the transaction will constitute (or must be carried out only by means of) a scheme of arrangement as contemplated in section 114(1), not that it is deemed to constitute a scheme of arrangement.”[173]

It is argued that section 48(8)(b) does not require share repurchases to be made by means of a scheme of arrangement, but parties may choose to use a scheme of arrangement to effect a share repurchase. Where this is done, the transaction will amount to an affected transaction. The Companies Act of 2008 however, is not specific whether or not such a repurchase “…now becomes an arrangement as contemplated in section 114.”[174] The legislature must make it clear that these transactions are not affected transactions. This is important particularly when one considers the numerous and cumbersome obligations

[169]Latsky (2014) *Stell LR* 381.
[170]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 208(1).
[171]208 (1).
[172]208(1).
[173]Latsky (2014) *Stell LR* 380.
[174]Luiz (2012) *PER/PELJ* 108/638.

relating to the concept of an affected transaction.[175] Yeats *at al*,[176] indicates that the effect of section 48(8)(b) is that the acquisition is treated as a scheme of arrangement and must accordingly comply with sections 114 and 115.

It may be asked whether it is necessary to import the requirements for a scheme of arrangement in respect of repurchases. It is submitted that the rationale for regulating such transactions is that by their nature, repurchases, like schemes of arrangement, have an expropriation effect and are potentially prejudicial to shareholders, even if the re-purchase is for a small percentage, such as five percent. Accordingly, it may be argued that shareholders need to be protected, and companies must comply with requirements for schemes of arrangements.

However, where parties merely repurchase shares on a consensual basis, such protections may be unnecessary.[177] Share repurchase may lead to unequal treatment of shareholders particularly where specified shareholders have their shares repurchased. Specified shareholders then have an undue preference to have their shares bought out at prices agreed with directors. In the case of specific repurchases it is possible that the repurchase may result in the wishes of the majority being forced on the minority. This abuse may be present particularly where the shares are tightly held and the market for them is less liquid. In this instance, the abuse will be that those shareholders who were not specifically approached to sell, will not have an opportunity to sell their shares elsewhere.[178] It will be sensible that the repurchase must be subject to additional protections for the minority shareholders. However, it is different where a company generally offers to repurchase shares from all its shareholders. In this scenario, only shareholders who wish to participate in the repurchase program will have their shares bought back by the company. No shareholder is forced to resell.[179]

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[175] 108/638.
[176] Yeats JL, de la Harpe RA, Jooste RD, Stoop H, Cassim R, Seligmann J, Kent L, Bradstreet RS, Williams RC, Cassim MF, Swanepoel E, Cassim FHI and Jarvis KA (2018) *Commentary on the Companies Act of 2008* 2-506.
[177] Latsky (2014) *Stell LR* 381.
[178] Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 203.
[179] See Latsky (2014) *Stell LR* 381.

Section 48(8) (b) is uncertain and lacks clarity.[180] The section does offer protection to shareholders as it curbs abuse by directors.[181] It appears that the protections to shareholders offered by section 48(8)(b) have been over-shadowed by problematic formulation and inaccurate targeting of the situations where problems may arise. It is again suggested that the provision must be amended for clarity and certainty.

5 6 6 An overview of additional requirements for fundamental transactions: section 115- Voting procedures and section 164- Appraisal Rights

This part provides an additional overview of some of the requirements for fundamental transactions. Disposal of all or the greater part of the assets or undertaking of a company in terms of section 112,[182] proposals for an amalgamation or a merger in terms of section 113 and schemes of arrangement in terms of section 114 of the Companies Act of 2008 are referred to as 'fundamental' transactions.[183] However, the term 'fundamental transaction' is not defined in the Act. Fundamental transactions contemplate major changes to the corporate substructure or essence of the business of the company proposing such a transaction. It is arguable that this is the reason why the legislature did not consider it necessary to define the term 'fundamental transaction': the term implies a major change to the shareholding in the company or the control over its assets. The requirements of section 115 of the Companies Act of 2008 must be met before fundamental transactions are implemented. Shareholder approval is necessary before the transaction may be implemented.[184] The approval is by a special resolution of independent

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[180] Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 203.
[181] 203.
[182] Section 1 of the of the Companies Act of 2008 defines 'All or the greater part of the assets or undertaking' as meaning more than 50 percent of the company's gross assets at fair market value, irrespective of its liabilities; or more than 50 percent of the company's value of its entire undertaking, at fair market value.
[183] See Part A of Chapter 5 of the Companies Act of 2008.
[184] Section 115(2) of the Companies Act of 2008.

shareholders.[185] However, if shareholders holding 15 percent of the votes at a meeting convened to vote on a fundamental transaction voted against it, the company must obtain court approval before proceeding with the transaction.[186] The company may also decide not to proceed with the transaction.[187] The requirement of a special resolution for fundamental transactions is there for good reason. As indicated earlier under paragraph 5 6 4 above, these transactions substantially affect the fundamental substructure of the company: additional protection for shareholders are required. For this reason, companies should not have authority to lower this requirement.[188]

The additional requirements for fundamental transactions are similar but depend on the type of affected transaction. It is only fundamental transactions that are also affected transactions that are subject to the jurisdiction of the Panel.[189] All fundamental transactions that are affected transactions must comply with the requirement for obtaining an independent expert to advise the shareholders about the value of the shares they are selling. The requirements for an independent expert for affected transactions other than a scheme of arrangement are not incorporated in the Act, but are found under regulation 90(1).[190] The requirements will only be applicable where a fundamental transaction is also an affected transaction. However, in the case of a scheme of arrangement, the requirement to obtain an expert report is applicable irrespective of whether the scheme is an affected transaction or not.[191] There may be an overlap in the application of the section 114(2) independent expert report for the scheme of arrangement and the expert report required by the regulations for affected transactions.[192] In the case of the disposal of assets or undertaking of the company, the independent expert should provide a valuation

[185]Section 115(4) of the Companies Act of 2008 read with section 115(4A)
[186]Section 115(3) of the Companies Act of 2008.
[187]Section 115(5) of the Companies Act of 2008.
[188]It is notable that section 115 (2)(b), indicates that the approval may be by a higher threshold as provided in the Memorandum of Incorporation of the company, but the section is silent on a lower threshold.
[189]Latsky (2014) *Stell LR* 363.
[190]See Latsky (2014) *Stell LR* 370 at note 48.
[191]Lasky (2014) *Stell LR* 369-370.
[192]370.

of the undertaking or the assets being disposed of.[193] Moreover, the overriding requirement appears to be that all shareholders are made aware of the protections offered to them in terms of section 115 and 164. The Companies Act of 2008 specifically requires that the independent expert report must include a copy of sections 115 and 164. This requirement is presumably intended to remind shareholders of their rights in terms of the Act.[194] These requirements are additional to other disclosure requirements for affected transactions in terms of the Takeover Regulations.[195] Further, the actions of directors undertaking the transactions are also subject to restrictions as discussed under paragraph 5 7 below. Regulation 89 provides for publication and delivery of notices to shareholders of companies involved in fundamental transactions.

The appraisal right is made applicable to all fundamental transactions.[196] The appraisal right in section 164 originated in the US.[197] It is aimed at assisting shareholders to exit a company whose risks may have changed and therefore no longer wish to stay invested in the company. It also serves to balance any bad business decisions that directors may make.[198] The appraisal remedy allows shareholders an opportunity to exit their company investment in return for payment in cash, but not to defeat a takeover or a merger. The section does not define 'fair value' or set out how 'fair value' must be determined. However, it indicates that the 'fair value' in respect of any shares must be determined as at the date on which, and time immediately before the company adopted the resolution that gave rise to a shareholder's right under the section.[199] Because the dissenters did not approve the event, any negative or positive effect on the value of their shares, should be excluded from calculating 'fair value'.[200] Increases or decreases are disregarded. This principle has been carried from

[193]Section 114(2) of the Companies Act of 2008 read with regulation 90.
[194]Cassim & Yeats "Fundamental Transactions, Takeovers and Offers" in *Contemporary Company Law* 663.
[195]Regulations 102 and 106 contain detailed disclosure requirements and the timelines within which steps must be undertaken. The assumption is that timely disclosures will assist shareholders in making informed decisions.
[196]Section 164 of the Companies Act of 2008.
[197]Cassim (2008) *SA Merc LJ* 157.
[198]Cassim (2008) *SA Merc LJ* 158.
[199]Section 164(16) of the Companies Act of 2008.
[200]See Delport *Henocshberg on the Companies Act 71 of 2008* 582.

Sammel v President Brand Gold Mining Co Ltd,[201] which is regarded a seminal case.[202]

The introduction of the appraisal right has been generally welcomed.[203] However, criticism has been levelled against a number of aspects of this new right. The efficacy of the appraisal right has been questioned due to its procedural flaws.[204] The appraisal right as set out in the Companies Bill was criticised for being too complex, technical and rigid for shareholders. It is associated with delays and prohibitive costs.[205] The appraisal right as contained in the Companies Bill remained substantially the same as in section 164 of the Companies Act of 2008. Therefore, these comments are still applicable. [206] Davids *et al*[207] share the view expressed by Cassim that the appraisal remedy may be costly to shareholders. They hold that this may discourage small shareholders with limited funding to exercise this right. An observation about this section is that it is one of the longest sections in the Companies Act of 2008, with subsections starting from 1 to 21. It is submitted that the section is complex and shareholders may find it difficult to exercise this right without requiring some expert advice.

The appraisal right as a remedy has not been very successful in those countries that have introduced it.[208] Many years before the appraisal right was implemented in SA, some of its critics had already indicated that:

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[201]1969(3) SA 629(A). In this case, the court dealt with a takeover scheme in terms of section 103ter of the Companies Act 46 of 1926, (currently, expropriation section 124 of the Companies Act), and held that the fair value should be considered without considering profit potential in future after the takeover, or any special value to the offeror, but the company's own profit potential as at the date of the takeover bid.

[202]See M Seligson "Dissenting Minority Shareholders' Appraisal Rights" (2016) 7:2 *Business and Tax & Company Law Quarterly*9.

[203]Cassim (2008) *SA Merc LJ* 157; and also, Davids et al (2010) *Acta Juridica* 337-338.

[204]Cassim (2008) *SA Merc LJ* 176.

[205]Cassim (2008) *Merc LJ* 164; and Cassim & Yeats "Fundamental Transactions, Takeovers and Offers" in *Contemporary Company Law.*

[206]Cassim (2008) *Merc LJ* 164. See also Cassim & Yeats "Fundamental Transactions, Takeovers and Offers" in *Contemporary Company Law* 807.

[207]Davids et al (2010) *Acta Juridica* 337-338.

[208]Cassim (2008) *Merc LJ* 157-168.

> "Altogether, the dissenter's appraisal statutes do not seem to work out very well in their practical administration. At best they are of modest and infrequent help to the dissenting shareholder, and they can be a distinct threat to others who have a stake in the enterprise."[209]

The appraisal right has also been criticised as a possible drain on a company's liquidity that may deter value-enhancing transactions. In addition, it is pointed out that it has limited power to keep managers' breaches of fiduciary duties in check, "because only large minority shareholders are likely to incur the legal expense required to exercise appraisal rights." [210] Of relevance to SA as an emerging market, the critics further hold that:

> "The appraisal remedy will surely work even worse in emerging markets than it does in developed markets. Yet there is no obvious alternative. Policing fairness through judicial or regulatory approval of major transactions is neither practicable nor desirable. Hence, one can only try to ameliorate the worst problems associated with appraisal rights. For example, a shareholder must actively oppose a transaction to qualify for appraisal rights. The shareholder must take a number of steps. In emerging markets, this condition weakens an already weak right. Given poor mail systems, shareholders may not learn of a transaction in time to vote against it or may find that their votes did not reach the company in time or were conveniently lost."[211]

Another criticism is that a shareholder seeking appraisal must go to court (an expensive process), without knowing in advance what the appraised value might be.[212] In that situation, the shareholders are at risk as they may not have all their expenses covered as they may receive a lower value than anticipated.

Companies tend to be wary of this right and it appears that South African practitioners have sought ways to avoid the application of this right. A better

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[209]B Manning "Shareholder's Remedy: An Essay for Frank Coker" (1962) 72 *The Yale Law Journal* 238.
[210]Black and Kraakman "A Self –Enforcing Model of Corporate Law" (1996) 109:19 *Harvard Law Review* 1056. 1056.
[211]1056.
[212]1056.

balance needs to be struck between protecting minority shareholders and facilitating economically advantageous transactions. Minority shareholders should not be allowed to hold up transactions against the will of the majority of shareholders who voted in favour the transaction.[213] Practitioners advise companies to introduce certain terms and conditions in takeover and merger documents, which, presumably, are aimed at protecting the interests of the offeror and avoid paying a higher price where shareholders exercise this right. These terms include a suspensive condition that should a certain percentage of shareholders (commonly five percent), exercise their appraisal rights and follow the appraisal right procedure to finality, the offeror reserves the right to terminate the takeover or merger transaction.[214] However, it is asserted that such conditions "neutralises the threat of uncertainty created by section 164 in relation to potential cash demands made by the shareholders in a target company."[215]

It is also asserted that in terms of section 6 of the Companies Act of 2008, dealing with anti-avoidance, a court and, in the case of a listed company, an exchange, has power to declare the particular condition or the entire offer agreement void. [216] Nevertheless, the issue will not be taken further here as it is beyond the scope of this dissertation. Researchers have pointed out the complexity of shareholders exercising appraisal rights as discussed. An interpretation and application by a court will assist shareholders in exercising the right.

In a recent matter, *Cilliers v La Concorde Holdings Limited (Cilliers case*),[217] a question of law was referred to the court in terms of Rule 6(5)(d)(iii) of the

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[213]Davids et al (2010) *Acta Juridica* 337-338.
[214]See Jinchuan Group Limited and Metorex Limited Circular to shareholder dated 2 August 2011 among other transactions.
[215]J Yeats *The Effective and Proper Exercise of Appraisal Rights under the South African Companies Act, 2008: Developing a strategic approach through a study of comparable foreign law* Doctor of Philosophy Thesis University of Cape Town (2015) 209.
[216]See Yeats *The Effective and Proper Exercise of Appraisal Rights under the South African Companies Act*, 2008: 209-214*.*
[217](23029/2016) [2018] ZAWCHC 68.

Uniform Rules of Court.[218] The court was required to determine whether or not shareholder appraisal rights were established in favour of a dissenting minority shareholder of a holding company, under section 164 of the Companies Act of 2008, where the holding company's subsidiary disposes of all or the greater part of its assets or undertaking, in circumstances where, having regard to the consolidated financial statements of the holding company, the disposal by the subsidiary constituted a disposal of all or the greater part of the assets or undertaking of the holding company referred to in section 115(2)(b) of the Act.

The court pointed out that section 164 created a right for a shareholder to exit the company, subject to compliance with certain requirements. The question is whether this appraisal right extends to the dissenting minority shareholders in the holding company. The court considered policy considerations for introducing the Act, including: (a) company law should provide remedies for investors;[219](b) it is an express policy objective to give meaning form and content to exit and appraisal rights and to provide smaller investors with the ability to make informed choices;[220] (c) the appraisal rights do not dilute or negate power of the majority, but seek to provide minority shareholders with equitable protection and fairness; [221] (d) the court concluded that a dissenting minority shareholder in the holding company is entitled to enjoy shareholder protection in the form of appraisal rights in terms of section 164 of the Act, where the disposal by the subsidiary constitutes a disposal of all or the greater part of the assets or undertaking of the holding company referred to in section 115(2)(b) of the Act.[222] The court further pointed out that section 115(8)[223] of the Act extends the category of shareholders to all other shareholders who have voting rights, that are not necessarily envisaged by section 164. Therefore, all

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[218]Rules Regulating the Conduct of the Proceedings of the Several Provincial and Local Divisions of the High Court of South Africa published under Government Notice R48 of 12 January 1965 as amended.
[219]*Cilliers case* at paragraph 42.
[220]Para 43.
[221]Para 44.
[222]Para 44.
[223]Section 115(8) of the Companies Act of 2008 provides as follows: "The holder of any voting rights in a company is entitled to seek relief in terms of section 164 if that person—(*a*) notified the company in advance of the intention to oppose a special resolution contemplated in this section; and (*b*) was present at the meeting and voted against that special resolution."

shareholders with voting rights, provided they complied with the relevant requirements, are entitled to seek appraisal rights in terms of section 164.[224] Despite criticisms against the appraisal right section, it remains one of the most important sources of protection for minorities. It is therefore necessary that the legislature simplify section 164 procedures by an amendment.[225]

5 6 7 Section 122 – The acquisition or announced intention to acquire beneficial interests in voting securities

The fourth affected transaction is defined as the acquisition or intention to acquire beneficial voting securities in terms of section 122(1). Section 122 is headed "Required disclosures concerning certain transaction". The section amongst other things requires that any party directly or indirectly acquiring or disposing of beneficial securities amounting to any multiple of 5 percent, 15 percent and so on, must notify the regulated company in the prescribed manner. The regulation provides prescribed forms for filing with the Panel by both the acquirer and the seller. The company receiving the notification must then notify its shareholders by means of an announcement and file a copy with the Panel. Regulation 82(2) provides for acquisition and disposals of securities in terms of section 122(1). The regulation states that acquisitions in terms of section 122(1) does not create any obligations for acquirers until an offer is made for all securities. The regulation merely confirms what is expected of acquirers when they make an offer to all shareholders and is in line with the definition of affected transaction in 117(1)(c). It is suggested that regulation 82(1) intends to clarify the obligations of certain parties and also the meaning of beneficial holders as contemplated in section 122(1). These include nominees or asset managers who have powers to dispose or vote on securities they hold.

The inclusion of acquisition of securities in terms of section 122 as affected transactions has been criticised. A closer consideration of the acquisitions in

[224] *Cilliers case* at para. 49.
[225] See also the observations by Cassim & Yeats "Fundamental Transactions, Takeovers and Offer" in *Contemporary Law* 807, and Davids et al (2010) *Act Juridica* 337-338.

terms of section 122 indicates that such acquisitions should not have been classified as 'affected transactions' but rather as disclosures. There are a number of problems in defining the transactions as "affected transactions". Section 122 transactions have two effects, as disclosures and affected transactions.[226] The classification of these acquisitions as affected transactions causes confusion and it imposes unnecessary and incongruous obligations on companies. It means that transactions that meet the requirements of section 122 will also have to meet the general requirements for affected transactions as set out in section 121.

Principally, this means that the transaction must be reported and be approved by the Panel. However, section 122 only concerns limited transactions (acquisitions in multiples of 5 percent) and limited obligations (to disclose and notify the acquisitions of the relevant percentages *to the regulated company*). There is no need for this type of wide-ranging Panel intervention in these limited circumstances. All other affected transactions or offers create obligations that various parties have to undertake such as: disclosure of certain information and take additional steps including, posting a detailed circular to shareholders; voting by shareholders; or acceptance or rejection of offers in other instances. Broader supervision by the Panel in these circumstances appear to be more appropriate.

Another problem is that the inclusion of the disclosure requirements as an affected transaction can be interpreted to mean that these transactions are 'partial offers' or 'offers', as defined in the Act.[227] The interpretation that the section requires an offer to be made, can have unintended consequences. For instance, an interpretation that an acquisition of five percent of the shares is an affected transaction, would also require that the acquirer must make a partial offer to acquire five percent of the issued shares from each shareholder.[228]

[226]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 429.
[227]N Boardman "A critical analysis of the new South African takeover laws as proposed under the Companies Act 71 of 2008" (2010) *Acta Juridica* 329.
[228]See section 125 of the Companies Act of 2008.This section deals with partial offers and comparable offer. It states that parties making such an offer must acquire on pro-rata basis from each shareholder.

Boardman[229] points out that this could lead to absurdity and such an interpretation is unworkable. The negative practical consequences could have been avoided if the stipulation had been properly identified as a mere disclosure requirement, instead of being within the definition of an affected transaction.[230]

The Panel has issued a Guideline 4/2011 on section 122(1). The guideline seeks to exempt companies undertaking transactions in terms of the section from obtaining a compliance certificate prior to implementing those transactions in terms of section 119(6), the general exemption section. As the Guideline indicates, it is acknowledged that it is not practical for companies to obtain the compliance certificate required by section 121(b)(i) prior to implementing the transactions. This purported exemption is arguably *ultra vires*.[231] In other respects, this section is in line with the requirements set in other countries where dealings in shares are disclosed. In the UK stricter threshold are imposed and notification to the authorities is also required.[232]

In conclusion, there are significant problems with certain aspects of the Companies Act of 2008, and this needs to be removed by amendment.[233] This section is just one of several provisions that needs attention.

5 6 8 The announced intention to acquire a beneficial interest in the remaining voting securities

The fifth affected transaction or offer is the announced intention to acquire a beneficial interest in the remaining voting securities of a regulated company not already held by a person or persons acting in concert in terms of section 117(1)(c)(v). The affected transaction under this provision is intended to apply to those situations where the parties make an offer for the securities of a company under circumstances where they own a certain percentage of the

229Boardman (2010) *Acta Juridica* 329.
230Sutherland (2012) *Stell LR* 173.
231Latsky (2014 Stell LR 362 at footnote 3.
232See UK Financial Services Authority (FSA) rules. In terms of the rule's investors are obliged to report to the company and to the FSA share dealing of 3 percent or every 1 percent complete thereafter in line with the EU Transparency Directives.
233Boardman (2010) Acta *Juridica* 330.

shares of the company, and they wish to acquire the entire 100 percent of the securities of the company. The section is aimed at protecting minority shareholders in a company where a shareholder makes an offer to the remaining shareholders in the company for all their shares. The offeror is obliged to comply with all the reporting requirements of the Takeover Provisions. The shareholders are protected in that they are not subject to any time pressures or forced to accept an offer that does not have clear terms and conditions.[234] The application of the section is not new as it was also applicable in terms of the SRP Code published in terms of the Companies Act of 1973.[235] The section may overlap with the mandatory offer in section 123 of the Act as discussed in the following paragraph below.

5 6 9   Section 123 -The mandatory offer requirement

5 6 9 1   Introduction

The mandatory offer requirement in terms of section 123 is listed as an affected transaction in terms of section 117(1)(c).[236] The mandatory offer requirement is the main focus of this dissertation. Accordingly, a detailed analysis of its application is undertaken in this part. The rationale for introducing the mandatory offer in South Africa is not easily discernible from research. Research on the mandatory offer provisions in South Africa is limited. Luiz, the leading scholar in this area, indicates that there is minimal literature specifically addressing mandatory offers in the context of South Africa. [237] At most it may be stated that the mandatory offer in South African law was initially based on the UK City Code.[238] It appears that the mandatory offer is one of the company law rules imported into South Africa to protect investors. The rationale for the

[234]See S Luiz "Protection of holders of securities in the offeree regulated company during affected transactions: general offers and schemes of arrangements" (2014) 26 *Merc LJ.* 570.
[235]See definition of "affected transactions" in the SRP Code.
[236]See the definition of affected transactions in paragraph 1 8 above.
[237]Luiz *An evaluation of the South African Securities Regulation Code on Takeovers and Mergers* LLD Thesis, Unisa. 727.
[238]S Luiz & K van der Linde "The mandatory offer obligation and intermediaries" (2011) *TSAR* 1.

application of the mandatory offer appears to be based on an incorrect application of the principles of the *Perlman case* relating to the sharing of a premium. It is asserted that the principles laid down in that case were specifically based on the unique facts of that case.[239] The history of the mandatory offer and its criticism is explored in detail below.

5 6 9 2 Development of the mandatory offer requirement

The Companies Act 46 of 1926 had the takeover offer and the scheme of arrangement procedure as methods of achieving takeovers.[240] Prior to the promulgation of section 103ter of the Companies Act of 1926, there was no statutory regulation specifically dedicated to takeovers and mergers in South Africa. This provision allowed squeeze outs where the offeror had obtained 90 percent acceptances from shareholders.[241] Accordingly, one of the first methods used for a takeover was a general offer, according to which the offering party could enforce compulsory acquisition after reaching 90 percent acceptance. The offer and acceptance methods were governed by common-law contract.[242] However, the scheme of arrangement was also used to facilitate takeovers. Each method had a different effect on protection of shareholders. First the protections are dissimilar and the choice of the method is often decided by the offeror, who will inevitably choose the method best suited for his interest.[243]

The scheme of arrangement became the preferred method for a takeover for a number of reasons. These include, the smaller majority required to achieve a complete takeover as opposed to the general offer, the shorter period required to implement the scheme and the certainty of the implementation. At the

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[239]See chapter 2 and the detailed discussions on the equal opportunity rule. In addition, see Katz (1997) *Journal for Juridical Science* 39 where he criticize, the application of the *Perlman case* as a basis for the mandatory offer.
[240]Luiz (1997) *SA Merc LJ* 242.
[241]242.
[242]SWL De Villiers “Takeovers Under Sections 311 to 321 of the Companies Act 1973” (1973) *SALJ* 351.
[243]IH Macgregor “Takeovers Revisited” (1978) 95 *S African LJ* 330.

meeting, the offeror will know whether shareholders vote in favour of the scheme or not, thus avoiding a long period as in the case of the general offer.[244] Unlike the general offer, the scheme results in complete takeover in one procedure and avoids uncertainties of waiting for shareholder acceptance of the offer.

The Commission of Enquiry into the Companies Act under the chairmanship of Mr Justice Van Wyk de Vries (Van Wyk de Vries Commission), whose report culminated in the Companies Act of 1973, was already concerned about the potential abuse that could occur where takeovers were effected by schemes of arrangements.[245] The important concern was whether the scheme procedure was being misused to avoid the take-over offer in terms of section 103ter of the Companies Act of 1926, the predecessor to sec 321 of 1973.[246] The scheme of arrangement had been introduced as a takeover method in the late 1960s in *In re National Bank Ltd*[247], an English court decision. The court sanctioned a scheme involving an outsider acquiring all the issued shares of a company. The scheme of arrangement contained in section 103ter of the Companies Act of 1926 was then used as a method to achieve takeovers in South Africa. The offeror could avoid the compulsory acquisition procedure by using the scheme of arrangement.[248] The Commission concluded that the fact that both the scheme of arrangement and the compulsory takeover offer could achieve the same commercial result was coincidental. It did not affect the legal principles involved. [249] The Van Wyk de Vries Commission introduced a number of changes to the takeover regulations. This commission considered regulation of takeovers for the first time in their Supplementary Report of 1972.[250] The changes included regulation of compromises, arrangements and takeovers.[251] The Commission also broadly considered methods of takeovers in the country,

[244]De Villiers (1973) *S African L.J* 350-352.
[245]See Chapter XXIV of the Supplementary Report (RP 31/1972). (Commission Report).
[246]See Luiz (2010) 22 *SA Merc LJ* 443.
[247][1966] 1 All ER 1006(ChD).
[248]Luiz “Some comments on the Application of the Securities Regulation Code on Takeovers and Mergers” (1997) *9 SA Merc LJ* 240.
[249]241.
[250]De Villiers (1973) *SALJ* 350.
[251]See Luiz (1997) SA *Merc LJ* 241.

principles underlying takeovers and the role of the Johannesburg Stock Exchange in supervising takeovers.[252]

The first statutory provisions regulating takeover schemes were sections 314 to 320 of the Companies Act of 1973. Compulsory acquisitions were included in section 321, while compromises and arrangements were incorporated in sections 311-313.[253] An offeror could achieve a takeover of a company by using the process in sections 314-320.[254] The takeover process could be completed by the compulsory acquisition of the shares of shareholders who did not accept the initial offer by using section 321.[255] Various methods of achieving a takeover were also used, including reductions of share capital subject to confirmation by court. The end result would be that the offeror would hold all the shares of the offeree company having cancelled some of the shares.[256] The statutory takeover offer was aimed at protecting individual shareholders when a change of control had occurred. The important aspect was the consideration to be offered. Shareholders were to be protected by being offered a fair price for their shares. It was felt that there should be fair dealing and protection from prejudice during the course of a takeover bid. Offerors had to provide shareholders with reliable information and sufficient time to consider such information. The Commission considered General Principle 3 of the City Code, which states that shareholders must be given sufficient information about an offer to enable them to make an informed decision in sufficient time. The obligation to provide the information is placed on directors. Directors are required to provide an honest and disinterested opinion about the merits and fairness of the offer consideration. Shareholders had to be able to rely on the information in the takeover offer statements.[257]

During the deliberations, the Commission considered it in the public interest that there was a statutory provision dealing with takeovers. The Commission

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[252]See Chapter XXIV of the Supplementary Report (RP 31/1972). (Commission Report).
[253]See De Villiers (1973) *S African L.J* 350-352 See also discussions by Luiz (1997) SA *Merc LJ.*240 -243.
[254]Luiz (1997) SA *Merc LJ.*241*.*
[255]241*.*
[256]242*.*
[257]De Villiers (1973) *S African L.J* 350-354.

also accepted that it was not possible to make rules for every situation that may occur during a takeover or a merger. The Commission favoured principle-based regulation. Therefore, it was believed that general principles had to be laid down for regulation of takeovers and mergers and that they had to be enforced by the JSE. In making recommendations for the regulations, there were also some concerns about including the monitoring and enforcement of a complex piece of legislation.[258]

The dearth of research on mandatory offers makes it difficult to ascertain the process leading to the adoption of the mandatory offer requirement. However, there is sufficient evidence to assume that the Commission's recommendations led to the introduction of the mandatory offer. The earlier recommendations from the Committee had already introduced some of the general principles of the UK City Code into the takeover offer procedure.[259] Even though the Committee considered some of the principles of the UK City Code for the takeover offer, it did not recommend the mandatory offer requirement at that stage. It is notable that equality of treatment of all shareholders was required for partial offers.[260] The effect of this was that the offeror would have to acquire a proportional number of shares from each shareholder to ensure equal treatment. It appears that this was the early stage of the introduction of the mandatory offer.

The mandatory offer in its more comprehensive form was introduced in South African company law in 1991 by means of chapter XVA of the Companies Act of 1973. Chapter XVA introduced the SRP Code as regulations to deal with takeovers and mergers. The chapter brought about major changes to the regulation of takeovers and mergers under the title "Regulation of Securities".[261]

[258]See Commission Report 31/1972 in paragraph 73.07. There is a suggestion that it may be difficult to police complicated takeover rules.
[259]See discussions by De Villiers (1973) *S African LJ* 364 above, on general principles 3 and 4 of the UK City Code.
[260]See De Villiers (1973) *S African L.J* 366.
[261]Luiz (1997) *SA Merc LJ* 242.

5 6 9 3 The mandatory offer requirement critiqued

The mandatory offer has been defined in paragraph 1 1 of the introduction above. The main thrust of the mandatory offer requirement is that the relevant person, usually a new acquirer, or acquirers, must cross the threshold of 35 percent of the voting securities of a regulated company through the acquisition transaction. The acquisition of more than 35 percent of the voting rights following an acquisition of the voting securities in a regulated company is regarded as a change of control for the purposes of section 123 of the Companies Act of 2008. This is not the same notion of control as is mentioned in section 2 of the Companies Act of 2008. The concept 'control' [262] as used in section 2 of the Companies Act of 2008 is related to *de facto* control through a shareholding of more than 50 percent, while the control relating to a mandatory offer refers to control of more than 35 percent of the voting rights of a regulated company as referred to under section 123, dealing with the mandatory offer requirements.[263] Section 123(5) refers to this shareholding as the "specified percentage" and set the threshold creating the mandatory offer. Luiz indicates that the definition of 'control' introduces confusion into the Takeover Provisions.[264] Moreover, the indiscriminate usage of the words "general voting rights", "voting securities" and "voting rights" is confusing due to the differences in their meanings and thoughtless use by the drafters of the Act.[265]

The architecture of the current South African mandatory offer differs substantially from the equivalent in the UK and in the Companies Act of 1973.[266] The Companies Act of 2008 focuses on specific types of transactions and classifies them as 'affected transactions'.[267] The transactions do not have to

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[262]See definition of control in Chapter 1 of this dissertation as extracted from the of the Companies Act of 2008.
[263]See 123 (5) of the of the Companies Act of 2008 which provides that "For the purposes contemplated in this section, the Minister, on the advice of the Panel, may prescribe a percentage of not more than 35 - percent of the voting securities of a company". See also the definition of control in Chapter 5 of the Takeover Regulations.
[264]See Luiz (2012) *PER/PELJ* 102/638.
[265]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 431.
[266]See Rule 9 of the UK City Code and also discussions by Luiz & van der Linde (2011) *TSAR* 125. The UK rule is discussed in chapter 3 above.
[267]Luiz (2012) *PER/PELJ* 103/683.

result in changes or consolidation of control.[268] The mandatory offer in terms section 123 of the Companies Act of 2008 is listed as one of the affected transactions.[269] The Companies Act of 1973 required that only a transaction that led to acquisition or consolidation of control, as defined, is an affected transaction.[270]

Commenting on the earlier SRP Code, Luiz and Van der Linde[271] point out that

> "The obligation to make a mandatory offer is made dependent on an arbitrary level of 'control', such as 30 percent or 35 percent, rather than on actual control. The ability to exercise or direct the exercise of voting rights is decisive for the South African definition of an acquisition of control, but not for a consolidation of control."

The mandatory offer has been justified in a number of ways, including that the minority should not be forced to remain in the company where there has been a change of control and a premium that has been paid to acquire control should be shared equally. The actual trigger of the obligation is not related to whether a premium is paid or not.[272] The initiator is the acquisition of the specific percentage threshold of beneficial interest in voting rights. It is not a specific requirement that a change of control has actually occurred or that a control premium has been paid.[273] The problem relating to payment of premium is certainly not easy to resolve. Legislation has extended the scope of the rule beyond its original purpose.[274] Based on this, Luiz[275] indicates that:

> "[A]n acquisition by a company of its own securities can even trigger a mandatory offer, without evidence of either a change of control or the payment of a premium."[276]

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[268] 103/683.
[269] 103/683.
[270] 103/683.
[271] Luiz & van der Linde (2011) *TSAR* 127.
[272] Luiz (2014) *SA Merc LJ* 569.
[273] E Wymeersch "The Takeover Bid Directive, Light and Darkness" (2008) *Financial Law Institute, Ghent University, Working Paper Series WP 2008–01* 5–6, Available at http://ssrn.com/abstract=1086987> *(Accessed* on 30-9-2013).
[274] 5.
[275] Luiz (2014) *SA Merc LJ* 569.
[276] 569.

The rule is triggered at different thresholds among EU countries. The rule raises considerable doubt with respect to its justification, its scope, rules of application and its wider externalities.[277] Many years into its implementation in EU countries, the arguments remain valid. In actual practice and in some respects, countries have followed different paths.[278] The mandatory offer rule appears similar but has quite different characteristics.[279] The mandatory offer is required even in cases where the controlling shareholder bought the shares on the market or from a number of shareholders who do not wish to control. In this scenario, control is not acquired but is 'created'. In these cases, no premium is paid, but the controlling shareholder is obliged to make an offer for all shares, although there is no transfer of a control premium.[280] Commenting on the projected revision of the Takeover Directive, Wymeersch suggests that the Takeover Directive should not only focus on a single factor such as the control premium, but should strike a balance "between flexibility, including contestability and stability and long term value creation, including in terms of human capital".[281] This suggests that takeover provisions should also allow for bidders to compete with each other among other considerations.

The SRP considered reasons for the application of the mandatory offer, over a number of months during 1996.[282] Some members asserted that the mandatory offer had the potential to inhibit good corporate governance and the reasons for its retention had to be re-examined. At a meeting of the SRP it was indicated that:

> "Members debated the philosophies of the premium attaching to control, minority protection from changes in management control and the equal

[277] E Wymeersch "A New Look at the Debate About the Takeover Directive" (2012) *Ghent University*, *Financial Law Institute Working Paper No 2012-05*.3.
Available at SSRN: https://ssrn.com/abstract=1988927.(Accessed 20 -5- 2018).
[278] 4.
[279] 3.
[280] 4.
[281] 3.
[282] Minutes of the SRP held on 28 May 1996 and 4 December 1996.

> opportunity and concluded that all the philosophies supporting the mandatory offer were flawed."[283]

Members also debated the introduction of the mandatory offer bid in the European Union, and the minutes indicate that:

> "The Panel cannot be out of line with international trends and it was agreed that the existing concept of the mandatory offers be retained in the Panel's Rules."[284]

The Standing Advisory Committee on Company Law (SAC) during 1997 considered the arguments for and against the mandatory offer. The SAC then decided to retain the mandatory offer as part of SA company law. The discussions of the SAC and retention of the mandatory offer was confirmed by the SRP at its meeting held during March 1997.[285] The SRP indicated that in view of the fact that the SAC has decided to keep the mandatory offer, the SRP also "…decided that the *status quo* would remain."[286] The SRP in two meetings favoured the retention of the mandatory offer although it was acknowledged that the mandatory offer had certain undesirable characteristics.

In deciding to retain the mandatory offer requirement, the SAC stated that the mandatory offer is... "generally seen as a measure to protect the minority shareholders."[287] The SAC offered the following justification to retain the mandatory offer: (a) shareholders should not be forced to remain minority shareholders without the option to sell their shares; (b) shareholders who are already minorities under a controller should not be forced to remain minorities under a new controller; and (c) 'looters', whose only aim is to gain control of the company and then sell its assets may be discouraged by the high cost of the

[283]Minutes of the SRP held on 4 December 1996. 2
[284]Minutes of the SRP held on 4 December 1996. 2
[285]Minutes of the SRP held on 4 March 1997. At this meeting, members of the SRP discussed the issue at length and agreed that the mandatory offers should be retained. Members also agreed to prepare a paper setting out the reason for retaining the rule.
[286]Minutes of the SRP held on 4 March 1997.
[287]M Larkin & J Boltar (1997) *Annual Surv S African* L 430.

takeover.[288] The obligation to make a mandatory offer increases the cost of a takeover substantially. The offeror must ensure that it has sufficient financial resources to buy out all the accepting shareholders. The Companies Act of 2008 seems to emphasise this requirement where it provides that parties must be "ready, able and willing" to implement the transaction.[289] While the SAC acknowledged the good intentions of the mandatory offer requirement, it also noted that there are convincing arguments against its application.[290] Some of the arguments mentioned by the SAC include: (a) the protection offered by the mandatory offer is not absolute as the controlling shareholder could sell the shares to avoid application of the then SRP Code and the mandatory offer requirement would not be applicable;[291] (b) the mandatory offer makes financing of a takeover offer extremely expensive; (c) the high costs of takeovers hampers the move toward black empowerment; (d) the current holders of economic power are in a position to further entrench their powers as only they, have financial resources to make a mandatory offer; and (e) 'looters' of companies will not necessarily be discouraged, as they will determine the price on the inherent value of the offeree company such that the mandatory offer price is not higher than the value of the offeree company. Under this circumstance, the takeover is still viable and they will still benefit.[292] Easterbrook and Fischel[293] reject the idea of a raid by an offeror having paid a premium to a majority shareholder and then subsequently 'looting' the company to the detriment of the minority shareholders. They point out that it is unlikely that an offeror will buy a substantial shareholding with a motive to 'loot' the acquired company without generating new value in the company.

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[288]431.
[289]See section 119 (2) (a) of the of the Companies Act of 2008.
[290]Larkin & Boltar (1997) *Annual Survey Company Law* 431.
[291]The sale referred to in the SAC minutes probably refers to a sale before the control threshold is triggered or an exemption has been granted. Rule 8.7 of the SRP Code allowed a transfer of shares from one party to another without triggering a mandatory offer where approval of independent votes was obtained.
[292]See Larkin & Boltar (1997) *Annual Survey Company Law* 431.
[293]FH Easterbrook & D Fischel "The Proper Role of a Target's Management in Responding to a Tender Offer" (1981) 94: 6 *Harvard Law Review* 1185.

A threat of a takeover might encourage good performance by managers.[294] Skilled and competent managers should manage companies. Mandatory offers however, could prevent this change. The mandatory offer also does not protect minority shareholders in all respects, because the requirement to make an offer on the same or equal consideration will encourage an offeror to reduce the offer price so that he is able to pay for the shares of all shareholders.[295] Only a full-blown competing bid guarantees that the best price may be obtained.[296] There is no obvious answer to the difficulties raised by the mandatory offer.[297] This is due to the fact that both its abolishment or retention has pitfalls. Abolishing the mandatory offer may make changes of control cheaper and easier. However, it may also have a negative effect of undermining the equality of treatment rule. In this dissertation, it is argued that the benefits of retaining the mandatory offer rule as it currently stands are less than the harms caused by it.

It is generally accepted that the mandatory offer requirement impedes BBBEE transactions due to costs.[298] It has been asked whether BBBEE should serve as a basis for abandoning the mandatory offer.[299] It has been submitted that even though BBBEE may be a laudable social and political goal, it should not be accommodated by interfering with the mandatory offer in order to reduce costs. BBBEE should be pursued by a cohesive economic strategy.[300] This dissertation argues that the mandatory offer requirement not only interferes with BBBEE policies, but is also a deterrent to good corporate governance as it prevents removal of inefficient managers by means of a change of control. This concern has been acknowledged by members of the SRP, as discussed above in this paragraph. In addition, the benefits of the mandatory offer cannot be determined with any degree of certainty, as indicated in this chapter and chapter 3, relating to the mandatory offer in the UK in terms of rule 9 of the City

[294]Larkin & Boltar (1997) Annual Survey Company Law 431-432.
[295]Luiz *An evaluation of the South African Securities Regulation Code on Takeovers and Mergers* 736.
[296]736.
[297]Luiz *An evaluation of the South African Securities Regulation Code on Takeovers and Mergers* 737.
[298]735.
[299]737.
[300]738.

Code. The SAC indicated that the arguments raised against the mandatory offer are also "very persuasive."[301] In addition, the offeror can avoid some of the rationales justifying the application of the mandatory offer requirement.

Corporate governance measures, such as, the mandatory offer applied successfully in developed countries are not necessarily a solution for developing countries, as pointed out by Armour *et al*.[302] In Chapter 3, relating to the UK mandatory offer it is generally accepted that the rule forms a cornerstone of protection of shareholders and operates well in the country. However, it has also been contended that its application in other EU countries has not been readily accepted. The success of the rule may be due to a number of reasons, such as: the type and size of capital markets; the ability to raise capital in those countries' capital markets; the size of the economies; the types and sizes of companies and shareholding structures, and social and economic developmental needs of those countries. The context within which laws are developed is very important. This is also important for developing countries that may be eager to adopt a particular set of rules with the hope that by adopting the best international practice, it would encourage inward investments. Capital market reaction to transplanted legislation differs from one country to another.[303]

5 6 9 4 Case law dealing with mandatory offers

There are only a few cases in South Africa that deal with affected transactions or offers. "It is seldom that a case concerning the interpretation of the Securities Regulation Code on Takeovers and Mergers (the Code) comes before the courts."[304] In *Sefalana Employees Benefits Organisation v Haslam*,[305] the court

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[301]See Larkin & Boltar (1997) Annual Survey Company Law 431.
[302]See DA Armour, S Deakin, P Lele & M Siems "How Do Legal Rules Evolve? Evidence from a Cross-Country Comparison of Shareholder, Creditor and Worker Protection" (2009) *ECGI Working Paper Series in Law Working Paper N°. 129/2009,* <http://ssrn.com/abstract=1431008> (Accessed on 14-4-2014).
[303]See S Deakin "Corporate governance, finance and growth: Unravelling the relationship" (2010) *Acta Juridica* 216-217.
[304]See Larkin & Boltar (1997) Annual Company Law Survey 427.
[305][2000] JOL 6205 (A)

indicated the issue “is as novel as it is narrow”.[306] In *Spinnaker Investments (Pty) Ltd v Tongaat Group Limited* the first case, dealing with takeovers and mergers, the court dealt with the provisions of section 314(2) of the Companies Act of 1973. The court set out the rationale for regulating “tender offers” or “takeover bids”:

> “The mischief whereby entrepreneurs operating on a big scale can gain control of a company by buying out one or two large shareholders and ignoring the small shareholders is to some extent curtailed. In a word, the operations of the financier, who is sometimes referred to in terms that are less flattering as a predator, a white-collar looter or an early-dawn raider are no longer unrestricted.” [307]

The court further stated:

> “The need for legislation to regulate tender offers or ‘take-over bids’ … has long been recognised since there is from time to time a sharp conflict between the interests of the offeror and the incumbent management of the offeree company … The shareholders in the offeree company may in consequence be prejudiced unless they are treated fairly and unless full and timeous disclosure of all relevant facts [is] made … to them and unless there is some form of sanction for dishonest statements and dishonest nondisclosure. Moreover, the directors of the offeree company often resist a take-over bid, because they wish to continue managing the company themselves instead of making way for the directors appointed by the successful offeror, or because they believe that the consideration offered for the share bid is inadequate. In this situation the only way the offeror can gain control of the company is by addressing an offer directly to its shareholders.”[308]

It is suggested that the arguments in the quotations above are not only applicable to mandatory offers but are applicable to the regulation of takeovers

[306] [2000] JOL 6205 (A) 2.
[307] 1982 (1) SA 65 (A) 71.
[308] 1982 (1) SA 65 (A) 71.

and mergers in general. They deal with fair dealing and proper disclosures during a takeover or merger on a much broader basis.[309]

In the *Sefalana case*, the Supreme Court of Appeal (SCA) endorsed the principles of protecting minority shareholders where a change of control occurs.[310] As indicated above, the enforcement of the mandatory offer is not a common occurrence. The matter was an appeal from an earlier decision of the High Court, where the High Court had ordered the appellant to make a mandatory offer to the respondent even though there was no actual change of control, because the party who would have acquired control repudiated the agreement to acquire control and the seller of control had accepted the repudiation. Briefly, the facts of the case that led to the appeal are: H, the plaintiff was shareholder in a company, Time Life Insurance Limited (Time). Sefalana Employee Benefit Organisation (SEBO), the defendant agreed to buy a controlling stake of 66 percent of the shares of Time from Concor Holdings (Pty) Limited (Concor). The agreement was subject to certain conditions that had been fulfilled. However, SEBO instead of continuing with the agreement to finality, repudiated and Concor, the seller, accepted the repudiation and the agreement was cancelled. It was generally accepted that the transaction fell within the definition of an 'affected transaction' of section 440A (1) of the Companies Act of 1973 and the SRP Code. The issue was whether the party who would have acquired control still had to make a mandatory offer in terms of rule 8.1 of the SRP Code, even though no change of control had occurred. The court of first instance agreed with the plaintiff that it did.[311] On appeal, the SCA ruled against the requirement of having to make a mandatory offer. The court also pointed that what must be appreciated from the beginning is that ordinarily, shareholders are not entitled to be treated equally when offers to purchase their shares are made. A purchaser who is aiming at acquiring control of a company,

[309]See section 119(1) and 119 (2) of the of the Companies Act of 2008 and Regulation 106 of the Companies Act 2011 (the regulations).
[310] [2000] JOL 6205 (A)
[311]*Haslam v Sefalana Employees Benefits Organisation* 1998(4) SA 964(W).

> "not in one fell swoop, but incrementally by way of a succession of purchases from different shareholders over an extended period of time, is under no legal or moral obligation to offer or to pay the same price from the inception of and throughout the exercise. It is only when the stage is reached at which an intended or proposed transaction will, if consummated, result in a change of control within the meaning of the Code that the hand of the panel is laid upon the transaction."[312]

The court pointed out the 'mischief' which the legislature tried to curb in enacting the mandatory offer referred to above in the *Spinnaker case.*[313]The SCA accepted the earlier decision by the High Court that the mandatory offer is directed, in the first instance, at actual takeovers and not aborted takeovers. An aborted or an attempted takeover of a company that does not succeed does not entitle minority shareholders to receive the mandatory offer. Partly, quoting from the decision of the High Court, the court observed:

> "[T] hat the would-be acquirer of control, ''abandons the booty when he or she resiles from the deal'', and that the minority shareholders "are left with shares they bought in the company, controlled as when they bought it." "[314]

The SCA further pointed out:

> "[C]ommon to all the situations under consideration is the stark fact that the sole rationale for the existence of an obligation to make a similar offer to other shareholders, namely, a transference of control, has fallen away prior to the making of an offer to them and there no longer exists any present prospect of the offeror acquiring control. Whose 'fault' that is (and there may be none) is of no consequence; the fact of the matter is that shareholders who were in jeopardy of finding themselves locked into a company the control of which has changed without their concurrence, are no longer in such jeopardy. The

[312] [2000] JOL 6205 (A) 6.
[313] See [2000] JOL 6205 (A) 9-10.
[314] [2000] JOL 6205 (A) 5.

mischief which the relevant provisions of the Act and the Code were enacted to counter is entirely absent."[315]

The SCA further held that:

"[T]he transaction envisaging a change of control was aborted before any offer had been extended to respondents, the rationale for making of a mandatory offer for respondents' shares no longer existed, and it would have been pointless to require an offer to be made to them. No discernible legislative purpose would be served by it."[316]

The SCA added that:

"[E]ven if there had been an acquisition of that nature, because it was cancelled prior to the making of any offer to respondents and without the *situs* of control having been disturbed in any way, no obligation to make an offer to respondents arose."[317]

Before ruling that no mandatory offer should be made, the SCA pointed out that:

"What all this shows, in my opinion, is that the coming into existence of a transaction or proposed transaction which involves the acquisition of securities which will, if implemented, result in a change of control within the meaning of the Code is a necessary, but not a sufficient, state of affairs to trigger the obligation to make an offer to other shareholders. Its continuing existence is a *sine qua non*."[318]

Luiz points out that the above assertion is not accurate due to the fact that the definition of affected transaction under the Companies Act of 2008 does not make "a change of control a *sine qua non* of an affected transaction."[319] The regulation of affected transactions under the Companies Act of 2008 seems

[315] [2000] JOL 6205 (A) 9-10.
[316] [2000] JOL 6205 (A) 13.
[317] [2000] JOL 6205 (A) 16.
[318] [2000] JOL 6205 (A) 20.
[319] Luiz (2012) PER/PELJ (15) 5.105/638.

more about the regulation of situations that could be viewed as changes of the fundamental nature of a regulated company. Regulation of affected transactions under the Companies Act of 2008 is not exclusively about the regulation of transactions which would result in a change or consolidation of control of the voting securities of the company.[320]

One of the difficult concepts to apply in regulating takeovers and mergers is the concept of parties 'acting in concert.'[321] The concept involves co-operation of two or more persons toward a common end or object.[322] The definition of the concept in the Companies Act of 1973[323] and according to Yeats et al, the SRP Code was also difficult to understand.[324] This was the case even though these definitions were based on the UK City Code as they were not identical. Yeats *et al*,[325] indicates that the UK City Code definition refers to a relationship between the parties. The concept 'acting in concert' is so defined because the City Code rules attach certain consequences to the existence of a relationship in terms of which persons are acting in concert. The rules treat the individual existing shareholdings of the parties to the agreement as the shareholdings of a single person and thus may oblige the parties to make a general offer where the holdings exceed the prescribed threshold of 30 percent.[326] The problem with the definition of 'acting in concert' in the Companies Act of 2008 is that it does not deal with the criticism raised in respect of the definitions in the 1973 Act and SRP Code, albeit that the detail regarding the problems with concept will not be discussed here as it would require too much of a digression. Suffice is to say that concert party agreements are difficult to prove and identifying exactly when shareholders 'co-operate for the purpose of entering into or

[320]Luiz (2012) PER/PELJ (15) 5.104/638-105/638.
[321]See Yeats et al *Commentary on the Companies Act of 2008* 5-47.
[322]5-46.
[323]Section 440A (1) of the Companies Act of 1973 indicates: **'acting in concert**' means, subject to subsection (2)(a) [of section 440A], acting in pursuance of an agreement, an arrangement or understanding (whether formal or informal) between two or more persons pursuant to which they or any of them co-operate for the purposes of entering or proposing an affected transaction. (Subsection (2)(a) deems certain persons to be 'acting in concert').
[324]See Yeats et al *Commentary on the Companies Act of 2008* 5-47.
[325]5-46 to 5-47.
[326]5-46 to 5-47.

proposing an affected transaction'[327] This led to the legislature trying to draft the concept as broadly as possible, using a catch-all approach.[328] Failure to draw a precise line could result in avoidance. Therefore, the definition still needs to be improved for certainty and clarity.

The court had to interpret the concept in the *Securities Regulation Panel v MGX Limited (MGX case).*[329] The matter was decided by the Witwatersrand Local Division of the High Court and concerned the mandatory offer. Prior to the court hearing the merits of the case, the parties had several legal skirmishes before the regulator – the SRP. The SRP finally brought an action at the High Court to enforce the obligation of the parties to make a mandatory offer to the shareholders of EC Hold Limited.

Briefly, the facts were that the plaintiff, the SRP, claimed that MGX Limited, the first defendant, and others, while "acting in concert", acquired more than 35 percent of the shares of EC-Hold Limited (EC-Hold) and became liable to make a mandatory offer to the minority shareholders of EC-Hold. Different persons acquired the shares, at different stages, but the combined acquisitions amounted to more than 35 percent of the shares of EC-Hold Limited. The SRP contended that the parties 'acted in concert' as contemplated in section 440A1(1) of the Companies Act of 1973. Accordingly, it requested the court to order the parties to jointly and severally make a mandatory offer to the shareholders of EC-Hold. After lodging its particulars of claim, the plaintiff applied to the court to have them amended and add further averments. The defendant objected against the particulars of claim on various grounds, including that the plaintiff: (a) failed to allege the term of the 'agreement, arrangement or understanding' which is necessary to hold the defendants as persons 'acting in concert' in relation to an 'affected transaction'; (b) failed to

[327]See definition of 'act in concert' in section 117(1) of the Companies Act 2008.
[328]See R Ghetti Acting in concert in EU Company Law: How Safe Harbours can Reduce Interference with the Exercise of Shareholder Rights" 2014.ECFR 4/2014 597-601. Discussion similar problems encountered in respect of the EU acting in concert definition. In this article, the author indicates the difficulties encountered in defining and limiting the application of acting in concert. It is indicated that concert party relations are generally hidden and difficult to prove. Identifying when exactly, shareholders are cooperating in order to circumvent a legal obligation may not be easy.
[329]*Securities Regulation Panel v MGX Limited* (the MGX case) Case No 1602/03.

allege that the defendant acquired shares in or control over the offeree company as contemplated by the definitions of acting in concert and affected transaction in section 440A; and (c) the particulars of claims are vague and embarrassing.

The court analysed the definition of 'acting in concert' and concluded that it is wide enough to include acts of co-operation that does not entail acquisition of shares. The court also indicated that the real issue is whether a party to an agreement, arrangement or understanding' who does not himself acquire shares in the offeree company can be a concert party if other parties co-operate to acquire shares. The court concluded that the agreement, arrangements or understanding covers a whole range of agreements and other acts falling short of legally binding contracts.[330]

The court also referred to the unreported case of *Randgold and Exploration Company Limited v Fraser Alexander Limited* (Randgold),[331] relating to an urgent application for an interim order. It distinguished the issues in the *MGX case* from those that were considered in the *Randgold case*. In the *Randgold case*, the court indicated that for control to have occurred in a case that relates to parties co-operating to vote together at a meeting, it must go beyond 'tomorrow's meeting'. The court indicated that the parties must have agreed to exercise control over the company at future meetings of the company. The fact that the parties had formed an alliance, which would result in them holding more than 40 percent of the shares and would give them management control in order to achieve the passing of a resolution the following day, was not sufficient to create an obligation in terms of the mandatory offer.[332]

In the *MGX case*, the court indicated that the "mere voting agreement" concluded in the *Randgold case* did not have the effect of vesting control, and, thus, it did not establish an affected transaction *per se,* due to the fact that the

[330]*Securities Regulation Panel v MGX Limited*, WLD Case No 1602/03.
[331]WLD, Case No 21801/94 ,17 August 1994.
[332]Case No 21801/94 17 August 1994.

effect of the voting agreement did not necessarily vest control of the company where it did not previously exist.[333] The court's decision shows that there had to be an ongoing, coordinated stratagem to control the company beyond a particular meeting. The MGX matter did not reach a final hearing on the merits of the case. The court dismissed the objections raised by the defendants during the preliminary proceedings. The main defendant eventually made a mandatory offer to the remaining shareholders of EC-Hold limited, even though a period of more than five years had elapsed after the obligation arose.[334] It is therefore argued that the shareholders of EC-Hold Limited did not receive 'fair and equitable' treatment as intended by the mandatory offer. The definition of 'act in concert' under the Companies Act of 2008 is not identical to the one under the Companies Act of 1973 and the SRP Code. The expression 'act in concert' is defined in section 117(1)(b) of the Companies Act of 2008[335] read with section 117(2), (which creates a rebuttable presumption). As discussed in this paragraph above, the concept is difficult to prove. Some of the concerns and ambiguities that arose under the Companies Act of 1973 may still persist.[336] As indicated by the discussions in this paragraph above, the concerns are reasonable.

5 6 10 Section 124 – Compulsory acquisitions and squeeze out

The seventh type of affected transactions is the squeeze out. The requirements of this section is applicable where the acquirer buys 90 percent or more of the shares that are the subject of the offer (excluding the shares already held by the acquirer). If the acquirer reaches the 90 percent or more, it may undertake a squeeze-out within 4 months after the date of the offer.[337] Making the compulsory acquisition under section 124 of the Companies Act of 2008, an

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[333] *Securities Regulation Panel v MGX Limited*, WLD Case No 1602/03.
[334] See EC Hold Limited. Announcement dated 20 April 2006, relating to the results of the mandatory offer as reproduced by JSE Limited SENS Department.
[335] Section 117(1)(b) defines the concept as: "'**act in concert'** means any action pursuant to an agreement between or among two or more persons, in terms of which any of them co-operate for the purpose of entering into or proposing an affected transaction or offer."
[336] Yeats et al *Commentary on the Companies Act of 2008* 5-51.
[337] Section 124(1) of the Companies Act 2008.

affected transaction ensures that the shareholders of the regulated company receive the protections available in the Takeover Provisions.[338]

Firstly, section 124 of the Companies Act of 2008 concerns so called 'squeeze outs.'[339] Such an acquirer will be entitled to expropriate any remaining shareholders who did not accept the initial offer under section 124(4). The expropriation must be done on the same terms and conditions as the initial offer.[340] The requirements of this provision is substantially similar to those which were applicable in terms of section 440K of the Companies Act of 1973, although the requirements of this section are phrased differently from those of its predecessor.[341] Oddly, squeeze outs are not expressly listed as affected transactions in section 117(1)(c) of the Companies Act of 2008, but the heading to section 124 of the Companies Act of 2008 includes a 'squeeze out'. This clearly is a mistake which requires amendment.

While the compulsory acquisition is defined as an affected transaction in its own right, it is argued that it is not possible to undertake an affected transaction in terms of section 124 of the Companies Act of 2008 without having undertaken either a mandatory offer in terms of section 123 of the Companies Act of 2008 or a general offer as described in paragraph 5 6 8 above, dealing with the announced intention to acquire the remaining securities. In addition, it is suggested that the time periods set out in terms of section 124 make it difficult to make an isolated section 124 compulsory offer in the absence of any other affected transaction.[342] In order to expropriate or squeeze out shareholders, the shareholders holding 90 percent or more must have accepted the initial offer. This will then entitle the acquirer to proceed and issue the requisite notices to expropriate those shareholders who did not accept the offer in terms of section

[338]See Luiz (2014) *SA Merc LJ* 581.
[339]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 434.
[340]Section 124(4)(c) of the Companies Act 2008
[341]Delport & Vorster *Henochsberg on the Companies Act 71 of 2008* 434.
[342]See section 124 of the Act. The provisions allow for a limited period of four months within which an offeror may subject to certain protections expropriate in terms of the section.

124(1)(b), unless they successfully challenge the expropriation in terms of section 124(2) by obtaining a court order.[343]

There is dearth of successful cases concerning these expropriations.[344] Section 124 further offers shareholders of the offeree company another opportunity to exit the company following the acquisition of 90 percent of the shares.[345] Under section 124(1)(b), the shareholders are entitled to exit the company on the same terms and conditions as the initial offer and therefore shareholders should not have a complaint.[346]

The rationale for the existence of the 'squeeze out' has been expressed as follows:

> "The legislature is concerned that the offeror, who may expend considerable sums of money in the expectation of acquiring total ownership of the shares in the target company, should not be prevented by a small minority of shareholders from acquiring total ownership of the shares and, if a corporate offeror, from converting the company into a wholly owned subsidiary, and so obtaining the commensurate and legitimate benefits financial, administrative and commercial that go with such ownership. In England, experience prior to the introduction in 1928 of legislation to facilitate by coercion of dissenting shareholders the amalgamation of companies, suggested that holders of small number of shares might, out of desire to exact better terms than the vast majority of their fellow shareholders were content to accept, hamper the arrangement or prevent it from materialising. Thus, the object of the legislation was, in effect, to prevent an oppression of the majority by a minority."[347]

The law protects shareholders who wish to exit the company, but it does not give a shareholder the right to stay invested in the company.[348] The right of a shareholder to insist that his or her shares be bought in terms of section

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[343]Section 124 of the Companies Act of 2008. See also Luiz (2014) *SA Merc LJ* 581.
[344]See Luiz (2014) *SA Merc LJ* 581.
[345]573.
[346]573.
[347]Yeats et al *Commentary on the Companies Act of 2008* 5-71.
[348]Luiz (2014) *SA Merc LJ* 585.

124(4)(b) despite not accepting the initial offer ensures that the minority shareholder can still exit the company at the original consideration paid. The shareholders of a regulated company that is subjected to a complete takeover seem to receive protection in terms of the section.[349]

5 6 11 Comparable and partial offers

5 6 11 1 Comparable offers

Comparable offers are regulated in section 125(2) of the Companies Act of 2008, and regulation 87 of the Takeover Regulations.[350] Section 125(2) is not easy to follow and apply. The SRP Code had similar provisions in rules 11 and 12. It is submitted that those rules were drafted better and easier to interpret and apply. Further, it seems that section 125(2) was derived from rule 11 of the SRP Code and some parts of rules 11 and 12 were inserted in regulation 88.

The Act and the regulations do not provide the meaning of comparable offer. The mandatory offer provision in section 123 of the Companies Act of 2008 does not deal with different classes of shares. It only refers generally to voting rights and voting securities. These provisions require bidders to make a comparable offer to the holders of voting securities in other classes where a mandatory offer is required. Accordingly, a person or persons acting in concert who acquires securities entitling that person or persons to exercise more than the prescribed percentage (currently 35 percent) of the general voting rights associated with all the issued securities of a company must make a comparable offer to acquire securities of each class of issued securities of that company.[351]

While the provisions do not define a comparable offer, regulation 87 sets out the circumstances that create an obligation for a comparable offer. These include: where a company has issued securities with voting rights or securities

[349]586.
[350]Section 125 (2) of the Companies Act of 2008 and regulation 87.
[351]See section 125(2) of the Companies Act of 2008 and regulation 87.

that could have voting rights in future, including options.[352] Share incentive schemes that are cash settled whose future value are dependent on the future value of the securities under offer, must be taken into account and receive an equitable treatment.[353] The offer consideration of a comparable offer must be established taking into consideration the class of security to which the comparable offer is to be made.[354] Regulation 90 generally creates an obligation for the independent board of regulated companies to obtain independent expert opinions for affected transactions and those opinions must then be disclosed in the offer circular. Regulation 87(5) creates a separate obligation for the independent board of regulated companies to obtain a fair and reasonable opinion relating to comparable offers. The opinions of the independent expert and independent board in respect of a comparable offer must accord with opinions of independent experts and the independent board expressed regarding the offer that gave rise to the comparable offer. In the case of comparable offers the regulation aims to achieve fairness for holders of the securities subject to a comparable offer. For example, if the opinion in respect of the primary mandatory offer is that the offer is 'fair and reasonable', then the opinion by the expert and the independent board in respect of the comparable offer must also be that the comparable offer is 'fair and reasonable'.

An obligation to make a comparable offer only arises in case of regulated companies that have more than one class of issued securities. The distinction between mandatory offers and comparable offers is that the mandatory offer is made on the same or identical terms and conditions as those that which were applicable when the acquirer reached the specified percentage,[355] while an offer in terms of section 125(2) is a 'comparable offer' as determined in terms of regulation 87. A comparable offer need not be an identical offer to the primary offer.[356]

[352]See regulation 87(2).
[353]See regulation 87(3).
[354]See regulation 87(4).
[355]See section 123(3) of the Companies Act of 2008 read with regulation 111 (2).
[356]See UK City Code in Rule 14.1 and the notes thereunder.

Luiz indicates that the requirements for a comparable offer support the goals for equivalent treatment and equitable treatment.[357] The requirements for comparable offers in terms of section 125(2) and regulation 87 serve an important role in protecting holders of securities identified in regulation 87. However, an amendment of section 125(2) and regulation 88 should improve interpretation and application of those provisions thereby offering better protection to those security holders.

5 6 11 2 Partial offers

The partial offer provisions are difficult to follow. Sections 117(1)(h) and 125 of the Companies Act of 2008 and regulation 88 provide for regulation of partial offers. However, despite partial offer being a defined term under section 117(1)(h) and regulation 88(2), the application of these provisions to partial offers is not clear.

(a) Partial offers in terms of section 125(3)

The Act under section 125(3) provides for offers that would result in the offeror (together with related persons and concert parties) owning less than 100 percent of a company's voting securities commonly, referred to as 'partial offers. Section 117(1)(h) of the Act defines a "partial offer" as an offer that, if fully accepted, would result in the offeror, alone or together with a related or inter-related person, or a person acting in concert with any of them, holding less than 100 percent of the voting securities of the company whose securities are the subject of the offer. This definition appears incomplete and section 125 sets both requirements for partial offers, but confusingly, also further defines what would constitute a partial offer. Section 125(3)(a) indicates that an offeror must make an offer to all holders of a class of securities. It would therefore require an offeror to make an offer to all shareholders but only for a proportion of their shareholding. A partial offer will only be regulated in terms of section 125 if it could result in an affected transaction. Although other offers could strictly be

[357]Luiz (2014) 26 *Merc LJ* 563.

partial offers, defining them as such will not have any legal consequences. The mere fact that an offer constitutes a partial offer will not make it an affected transaction. A partial offer will only be regulated in terms of Chapter 5 Part B if it is an affected transaction because it falls within one of the categories set out in section 117(1)(c), which could be that it would otherwise trigger the mandatory offer in terms of section 123 or that it would mean that one of the thresholds mentioned in section 122 would be crossed. Offers under section 125(3) includes acquisitions of small stakes that would take a shareholder across one of the disclosable dealing thresholds such as 5, 35 or 50 percent provided for under section 122.[358]

This section, if taken on its own, would be problematic when small acquisitions are made. It is difficult to see why this provision should apply where an acquirer or acquirers do not acquire control. Most of the requirements in section 125(3) would apply only where the prescribed percentage has been or could be crossed. It is only in these situations that: (a) the offer will have to be conditional on a specified percentage of acceptances;[359] (b) the offer must be approved by independent holders of securities;[360] (c) the offer must be for a specific percentage if it could also result in the offeror holding less than 50 percent of the voting rights;[361] (d) a notice to this effect has to be given.[362] In this sense, the impact of section 125 is limited, albeit that it is still overly wide.[363]

Firstly, offerors who already have acquired the prescribed percentage may have to comply with some of these requirements in circumstances where it would not make much sense. These transactions will not be affected transactions in terms of section 123 but they could be for other reasons, such as, the crossing of the 5 percent thresholds. Under this scenario, the shareholder would already have made a mandatory offer and yet the partial offer provisions will still apply. This will be the case both where more than 35

[358]See Boardman *Acta (2010) Juridica* 328.
[359]Section 125(3)(b)(i) of the Companies Act of 2008.
[360]Section 125(3)(b)(ii). of the Companies Act of 2008. See the discussion below.
[361]Section 125(3)(c) of the Companies Act of 2008.
[362]Section 125(3)(d) of the Companies Act of 2008.
[363]Boardman (2010) *Acta Juridica* 330.

but less than 50 percent of the voting rights has previously been acquired, and even where more than 50 percent has previously been acquired.[364] Secondly, and more importantly, the requirement that a partial offer will have to be made to all shareholders will apply more broadly to all partial offers that are affected transactions for reasons other than section 123.[365] This will be the case at very low shareholding but also where the prescribed percentage had already been crossed previously. A very small acquisition that crosses a low threshold such as 5 percent could mean that a general partial offer will be required.[366]

Regulation 88 provides that a partial offer is exempt from compliance with part B and Part C of Chapter 5 of the Act and the regulations: (a) if at the time the partial offer is made, the offeror beneficially holds securities of a class with voting rights of less than the prescribed percentage and the partial offer is limited to the acquisition of less than the prescribed percentage; or (b) where the offeror already holds voting securities equal to or more than the specified percentage and makes a partial offer to acquire less than 100 percent of the voting rights. The partial offers covered by the exemption in the regulation are those that at the time at which they are made, either will not result in the offeror acquiring voting rights of more than the specified percentage, or are those partial offers where the offeror already holds voting rights of more than the specified percentage but will not be acquiring the entire voting rights of the regulated company.

In the first scenario the mandatory offer requirements in section 123 has not been triggered and there is no reason to provide exclusion from the mandatory offer as envisaged in section 125(3). Presumably, in the second scenario, the offeror would have complied with the mandatory offer obligations at some earlier stage or would have crossed that threshold in some legitimate manner at some stage of their share acquisitions. As an example, The Bidvest Group Limited (Bidvest) acquired 34.5 percent of the shares in Adcock Ingram Holdings Limited without involving the Panel. The parties appear to have relied

[364]See Boardman (2010) *Acta Juridica* 331.
[365]Section 125(3)(a) of the Companies Act of 2008.
[366]See Boardman (2010) *Acta Juridica* 331.

on this regulation and did not comply with the Takeover Provisions. The offer was undertaken by means of a “stand-by offer” (a public announcement offering to acquire the shares of the offeree company on the terms and conditions set out in the announcement) by Bidvest. This meant that it did not have to involve the Panel, as the transaction was not subject to the Takeover Provisions.[367]

Although the Act does not say so explicitly, it would seem that section 125(3) read with the regulation is intended to provide an exclusion from the mandatory offer requirement in section 123 for offers that fall within section 123(2), which determines when section 123 would ordinarily apply.[368] It concerns offers that would have triggered the full mandatory offer in terms of section 123 but will no longer do so if the requirements of section 125 are met. Although at first glance section 125(3) expands regulation, it in reality provides relief from the strict requirements of section 123. For this purpose, the most important requirement for the protection of offeree shareholders is section 125(3)(b)(ii). It requires that the partial offer be approved by independent shareholders.

Nevertheless, the provision is badly formulated. It could also be read that it requires that independent shareholders who support the offer must hold more than 50 percent of all votes in the class and not just of the independent votes. The requirement will then be more difficult to meet where shareholders that are not independent have larger shareholding than it would be if they have smaller or no shareholding. Where the independent holders will no longer have 50 percent, it will mean that the requirement can no longer be met. This would lead to the arbitrary outcome that offerors with large existing holdings will not be able to make partial offers while ones with smaller shareholding would be able to do

[367]See Announcements released by The Bidvest Group Limited and Community Investment Holdings Pty Limited (the Parties) dated 2 December 2013 in which the Parties offer to acquire a maximum of 34.5 percent of Adcock Ingram Holdings Limited (Adcock) shares. In this announcement, Parties offer to acquire the shares of Adcock from the shareholders at R70 .00 per share on a first come first served basis. The offer period closed on 4 February 2014. The Parties in their announcement dated 31 January 2014 indicated that they acquired 32,03 percent, short of their intended target of 34.5 percent. It must be pointed out that the offer was completed outside the regulatory oversight of the Takeover Provisions as no circular approved by the Panel in terms of the regulations was sent to the shareholders of Adcock. What is also notable is that the time period for the notice to close the offer was very short leaving shareholders with little time for accepting the offer.
[368]Boardman (2010) *Acta Juridica* 328.

so. Perhaps it would be better to interpret the approval requirement in the first part of the provision as being independent from the second part that refers to holding of 50 percent by independent holders. If so, understood approval by majority will be required only where the independent holders still have 50 percent of the voting rights in a class but that no approval will be required where this is not so. Where the offeror and related parties control more than 50 percent of the voting rights no approval would be required.

Where there is a vote on a partial offer, the offeror must advise shareholders in a specific and prominent notice that it would be able to exercise more than the prescribed percentage of the general voting rights of all the issued securities of the company, in the circular that is provided to shareholders before they approve the partial offer.[369] Through this notice, shareholders are made aware that they will be forgoing the right to receive the mandatory offer before they vote in favour of the partial offer. The disclosures and voting required in terms of section 125(3) are aimed at protecting the interests of shareholders. Shareholders must be made aware that the partial offer may result in shifting of voting control to a new majority shareholder. The voting in favour of the partial offer by a majority of the independent shareholders aims to remove conflicts and oppression by the existing majority shareholders.

Section 125(4) requires the exact percentage indicated in the partial offer to be achieved before the offer is declared unconditional as to acceptances. This is important as the implementation of the partial offer is predicated upon the condition being fulfilled. This also promotes transparency, as shareholders will know the exact number of shares held by the controlling shareholder.

(b) Section 125(5)

Section 125(5) of the Companies Act of 2008 concerns how a shareholder may tender shares in terms of a partial offer. In terms of this provision, the holders of different classes of securities are entitled to accept the offer in full for the

[369]Section 125(3)(d) of the Companies Act of 2008.

relevant percentage of that person's securities holding. If all shares that are offered are not taken up in this way, any securities tendered in excess of the relevant percentage must be accepted by the offeror from each holder of securities in the same proportion to the number tendered as will enable the offeror to obtain the total number of shares for which it has offered to accept. Regulation 88(3) also assists in ensuring that shareholders are treated equally in a partial offer. It provides that where shareholders tender their acceptance for equal or less than the partial offer, then the offeror must accept all their shares. This again seems to merely confirm the statute when it comes to acceptance of an offer to its full extent, while it probably clarifies the position where a shareholder agrees to take up less shares than those offered. Finally, the regulation determines that if a shareholder tenders shares more than the partial offer percentage, then the offeror must accept that number of shares equal to the partial offer percentage, and accept the excess tendered by shareholders on an equitable basis.

It would appear that regulation 88(1) will impact on the application of section 125(5). It will mean that both the statute and the regulation regarding the manner in which shares purchased in terms of a partial offer will have to be taken into account.

(c) Comparison with the UK City Code

In the UK, rule 36 of the UK City Code deals with partial offers.[370] The SA section 125(3)-(5) of the Companies Act of 2008 is very similar to rule 36 of the City Code. The UK City Code does not only concern partial offers that would otherwise be subject to the mandatory offer requirement. The UK Panel's consent is required for any partial offer in terms of rule 36.1. In South Africa, partial offers that are not affected transaction are not subject to approval by the Panel.[371]

[370]UK City Code (2016).
[371]See Regulation 88

This means that approval in the UK will be necessary, even where the partial offer does not cross the mandatory offer threshold of 30 percent, although these transactions will not be covered in section 125(3) of the Companies Act of 2008. However, the Panel will normally grant such consent where the partial offer will not result in the offeror holding 30 percent or more of the voting rights of a company.[372]

Moreover, where the UK Panel gives approval, the mandatory offer requirement will not have to be met even if the mandatory offer threshold is passed.[373] However, approval will not be given where the offeror has selectively or in significant numbers, acquired interests in shares in the offeree company during the 12 months preceding the application for consent or if interests in shares have been acquired at any time after the partial offer was reasonably in contemplation.[374] In this sense, approval will have the same effect as compliance with the section 125(3) of the Companies Act of 2008. Rule 36.6 of the City Code provides that if the partial offer could result in the offeror and concert parties holding shares carrying over 50 percent of the voting rights of the offeree company, the offer document must include 'specific and prominent reference' to this fact. Further, the offer document must state that, if the partial offer succeeds, the offeror 'will be free', subject to other relevant rules to acquire further interests in shares without incurring any obligation to make a mandatory offer under Rule 9. While section 125(3) contains similar requirements, it does not go further and provide that the offer document must inform shareholders that the offeror would no longer be obliged to make a mandatory offer.

Under rule 36.7 of the City Code, the offeror must accept tendered shares proportionally and those who wish to sell more or less must be able to do so. South Africa in section 125(5) and regulation 88(3) contains similar provisions. In the UK, offerors must not acquire additional shares during the offer period and further, for a period of 12 months, offerors must not acquire further shares

[372]See rule 36.1 of the UK City Code (2016).
[373]See rule 36.2 of the City Code (2016).
[374]Rule 36.2 of the UK City Code.

in the offeree unless the Panel consent,[375] and in SA, a similar provision is found in section 127(4). Although it does not specifically refer to the SA Panel's consent, it is possible for offerors to obtain such consent from the SA Panel in terms of the SA Panel's general powers to provide exemptions.[376]

(d) Conclusion

Section 125(3)–(5) of the Companies Act 2008 deals with partial offers where the offeror either does not have sufficient resources to acquire 100 percent of the securities of a company or where it chooses to do so for its own reasons.[377] The main benefit for offerors launching a partial offer therefore will be that it can provide the flexibility of not having to buy the whole company.[378] One of the main concerns is that partial offers may not necessarily treat all shareholders equally and may create minority interests.[379] In the UK, partial offers are not favoured.[380] Partial offers are seen as unfair and oppressive to shareholders. It has been suggested that shareholders can be coerced into accepting a partial offer even if they did not believe the offer to be fair.[381] In South Africa, there will now be wider scope for these partial offers than in the UK.[382] The SA approach is favoured as it reduces the impact of the mandatory offer which has been submitted to criticism in this thesis.

Section 125 allows considerable scope for partial offers. This could substantially restrict the impact of the mandatory offer requirements in South Africa. It is debatable whether there is a need to protect shareholders in case of partial offers by offerors who already have crossed the control threshold. Currently, protection for minority shareholder is under section 122 dealing with disclosures of acquisition of shareholdings of 5 percent, 10 percent or 15 percent and so on and, also under section 117(1)(v), as discussed above in

[375]Rule 36.3 of the UK City Code.
[376]See section 119(6) of the Companies Act of 2008.
[377]See Yeats et al, *Commentary on the Companies Act of 2008* 5-81.
[378]Boardman (2010) *Acta Juridica* 328.
[379]328.
[380]See Boardman (2010) *Acta Juridica* 329.
[381]I Ramsay "Balancing Law and Economics: The *case of Partial Takeovers"* (1992) *Journal of Business Law* (369-397, 370.
[382]Boardman (2010) *Acta Juridica* 330.

paragraph 5 6 7, indicating that offerors who wish to acquire 100 percent of the voting securities in a regulated company, must comply with the requirements for affected transactions. Some of the requirements in terms of section 125(3) require clarification. The insertion of rule 36 of the City Code into section 125(3)(c) creates confusion due to the fact that the South African mandatory offer requirements apply only until a person acquires 35 percent or more. Once a person has acquired that percentage, any further acquisitions above 35 percent does not result in a further mandatory offer. In the UK the threshold is both 30 percent and 50 percent as discussed under paragraph 3 2 3 above, hence the requirement that offerors must disclose their shareholding position prominently.[383] In the UK, this assists shareholders to determine which threshold has been reached, 30 percent or 50 percent. In this way, shareholders are informed about the threshold that created the mandatory offer. Shareholders can then choose to tender or not tender their shares knowing who the controlling shareholder is.

In SA, the reference to 50 percent under section 125 is not relevant for the purpose of mandatory offer but may assist shareholders to establish if the offeror desires to acquire legal control. It also promotes transparency about controlling shareholders. Regulation 88 addresses some of the problems with the partial offer provisions but it has rightly been criticised from certain quarters. It is indicated that section 123 creates a mandatory offer obligation and regulation 88 appears to be *ultra-vires* as it seeks to exempt a category of “partial offers”' as provided for by section 125(3) of the Act.[384] Even if the Regulation is not ultra vires, the exact impact of the exemption of partial offers requires refinement and the formulation of these provisions must be amended to promote clarity and ease of application. It is preferable that section 125(3)-(5) be amended rather than provide exclusions in terms of a regulation.

[383]Rule 36 of the UK City Code (2016).
[384]Latsky (2014) *Stell LR* 362.

5 7 An overview of the conduct regulated: restrictions before, during and after affected transactions and offers

Some of the provisions in this section have been taken from the SRP Code and are word for word the same as those in the SRP Code.[385] The general principles, previously in the SRP Code, have now been elevated to statutory provisions.[386] The general principles have been described in paragraph 5 4 above.

This paragraph highlights some of the restrictions in terms of the Takeover Provisions and provides the reasons for such restrictions. Takeovers and mergers of companies are a common occurrence in commerce but are fraught with problems and potential conflict of interests. Conflicts may arise where the offeror attempts to acquire the shares at the lowest price possible as opposed to the shareholders who may wish to sell their shares or assets or undertaking of the company at the highest price possible.[387] Conflicts could also arise between majority shareholders and minority shareholders. In addition, incumbent management also poses a problem during an affected transaction, as they may wish to secure their positions to the detriment of shareholders.[388] This appears to be one of the main aims of regulating takeovers and mergers by various regulatory authorities in different countries. Conflicts specifically involving directors require policing in order to safeguard the interest of shareholders during takeovers and mergers.[389]

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[385]See Rule 19 of the SRP Code.
[386]Luiz (2014) *SA Merc LJ* 563.
[387]See Luiz "Protection of holders of securities in the offeree regulated company during affected transactions: general offers and schemes of arrangements" (2014) 26 *SA Merc LJ* 561.
[388]Luiz (2014) *SA Merc LJ* 560.
[389]For Delaware, see chapter 2 dealing with standards of reviewing directors conducts during takeovers applied by the Delaware courts. For the UK, see chapter 3, the UK Panel rule 21.1 of the City Code set a no frustrating rule in as part of board neutrality rule to curb conflicts of interests by directors. Finally, for Australia, see chapter 4. In particular paras 4 2 3 1 and 4 2 3 2 for ASIC and the Australian Panel respectively. The power to declare unacceptable circumstance by the Panel discussed in para 4 2 4 above is also potent and effective in preventing conflicts of interests by directors.

Section 121 of the Companies Act of 2008 creates an obligation for parties entering into affected transactions or offers that may result in affected transactions, to report them to the Panel.[390] Such transactions must not be effected unless they have been approved by the Panel or have been exempted from approval by the Panel.[391] Section 121 also specifically provides that parties must not enter into such transaction unless they do so in accordance with the general requirements of the Companies Act of 2008 and Panel regulations. The earlier intervention by the Panel limits the potential prejudice to shareholders. For instance, a refusal by the Panel to approve a particular transaction before the transaction is announced on the market, reduces the risk that shareholders may trade in shares of a company to their prejudice. This is particularly true where the offeror is not able to fulfill its financial obligations in terms of the offer.[392] The rationale for prohibiting certain actions by directors is aimed at protecting shareholders' interests. Directors may impede a beneficial transaction for shareholders which prejudice the directors' interests. A requirement to disclose under various regulations including regulation 106, and the requirement of a shareholder vote on some transactions, for example under section 125(5) and regulation 86(4), ensures transparency and avoids conflicts of interests. The procedures further enable shareholders to make informed decisions about affected transactions.[393]

The Companies Act of 2008 also prohibits actions that may frustrate or prevent affected transactions or offers, unless shareholder approval and the written approval of the Panel are obtained in terms of section 126(1).[394] Section 127(1) of the Companies Act of 2008 prohibits certain dealings during an offer. These include any favourable or collateral benefits from being paid to some securities holders during the course of an offer unless all securities holders are paid the

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[390]See definition of offers under section 117(1)(f) of the Companies Act of 2008.
[391]Section 121(*b*) of the of the Companies Act of 2008.
[392]See section 119(1) of the Companies Act of 2008 and regulation 111 dealing with requirements for bank guarantees and cash confirmations where parties are paying in cash.
[393]See section 126 of the of the Companies Act of 2008.
[394]This provision is similar to Rule 19 of the SRP Code referred to above and the wording is almost the same.

same.[395] Prohibition of collateral benefits is intended to ensure that shareholders are treated equitably and fairly. Section 127(3) prohibits the offeror making another offer, or an offer that may require a mandatory offer for the shares of the company being made within a period of 12 months, in a situation where the initial offer has failed. The UK City Code, has similar restrictions.[396] The UK Panel may consent and allow an offeror to make another offer in a number of circumstances. These include: where there is a competing offeror; where it determines that there has been material change of circumstances; or where the board of the offeree company recommends the new offer except in case where the initial offer closed within three months of such new offer and the offeror had indicated that it will not increase the initial offer. [397] The Panel is likely to follow a similar approach taking into consideration the provisions of section 119(6) of the Companies Act of 2008, in particular, 119(6)(c), as discussed under paragraph 5 11 below. The UK City Code will also be useful in considering whether the Panel must relax a requirement, in particular, the explanatory notes under the various rules of the UK City Code are likely to be persuasive.

It is asserted that restrictions following a transaction are intended to stabilise the operations of a company following the completion of an offer. This is necessary due to the fact that, during the course of the offer, directors of the offeree company have numerous obligations to ensure compliance with the Act and the regulations. During this period, the operations of the company may not receive undivided attention, to the detriment of shareholders' interests. According to Pudge, the restriction in the rule is aimed at preventing a 'siege' being renewed immediately within 12 months.[398] This rule is designed to create

[395]For the purpose of this section the important consideration is the definition of the "offer period". This period is defined as the period "from the time when an announcement is made or ought to have been made, of a proposed or possible offer until the first closing date or, if later, the date when the offer becomes or is declared unconditional as to acceptances or lapses" in section 117(1) (*g*)) of the Companies Act of 2008.
[396]See UK City Code Rule 35.
[397]see UK City Code rule 35 and notes thereunder.
[398]D Pudge "Conduct During the Offer, Timing and Revision; and Restrictions Following the Offer" in Button (ed) *A Practitioners' Guide to the City Code on Takeovers and Mergers. City & Financial Planning* 274.

a reasonable balance between giving shareholders an opportunity to consider offers for their shares and enabling the business of the company, in which they are invested in, to be carried on without continuous uncertainty and disruptions.[399]

Another restriction in dealing with the shares of the target after an offer is completed, is found in section 127(5). The section restricts the offeror from acquiring shares in the company on more favourable conditions than was offered during the original offer for a period of 6 months following the closing date of the offer. The section is aimed at fostering equality of treatment and preventing offerors acquiring shares at a higher price immediately after the closing of the offer. It therefore promotes fairness and equity in line with section 119(2) (b) of the Companies Act of 2008. The restriction may also have the effect of stabilising the share price of the offeree company as any selling shareholder will be aware of the restriction. Therefore, the possibility that the share price will immediately rise or fall after the termination of the offer may be reduced.

5 8 An overview of the remedies and enforcement measures

The Companies Act of 2008 provides a number of ways for the Panel to enforce compliance with affected transactions and offers, and sets out the consequences of failure to comply. The Companies Act of 1973 also provided mechanisms for enforcing compliance in sections 440L and 440M.[400] Section 440L of the Companies Act of 1973 required that every affected transaction had to be proposed or entered into in accordance with the Act, unless exempted. Section 121 of the Companies Act of 2008 now states that the transactions must comply with certain reporting requirements, unless exempted. In addition, the section provides that transactions must not be implemented unless the Panel issues a compliance certificate or the transaction is exempted. The Companies Act of 1973 did not specify that the SRP must approve transactions.

[399]275.
[400]Chapter XVA of the Companies Act of 1973.

Moreover, the Takeover Regulations now specifically provides that the Panel must approve announcements and circulars in respect of affected transactions.[401]

The Companies Act of 1973 did not create enforcement measures that could effectively deter potential transgressors. Section 440M of the Companies Act of 1973 provided that the SRP must approach the courts to enforce compliance where there was a contravention or possible contravention. In addition, section 440M (4) provided that persons who suffered damages due to non-compliance could claim damages. However, concerns were raised that remedies and enforcement procedures were unsatisfactory.[402] They were described as ineffective, lacking clarity and certainty, and without any deterrence.[403]

The Companies Act of 2008 goes a long way to address these concerns by introducing a number of remedies and enforcement procedures. Persons who believe that they have been harmed by an affected transaction have a number of remedies. In addition, the powers of the Panel to enforce have been clarified and bolstered. The Panel may issue a compliance notice in terms of section 119(4), where there is non-compliance. Section 119 of the Companies Act of 2008 provides that:

> "(5) To the extent necessary to ensure compliance with this Part, Part C and the Takeover Regulations, and to fulfil the purposes contemplated in subsection (1), a compliance notice contemplated in subsection (4) (c) may, among other things— (a) prohibit or require any action by a person; or (b) order a person to— (i) divest of an acquired asset; or (ii) account for profits."

The section goes considerably beyond section 440M of the Companies Act of 1973. The Panel may issue a compliance notice and will only have to revert to the National Prosecuting Authority or the courts if there is no compliance with the notice.[404] These steps are necessary to ensure speedy and effective

[401] See Regulation 117.
[402] DTI 2004 Policy document.
[403] DTI 2004 Policy document
[404] Sections 119(5) (b) and 171 of the Companies Act of 2008, read with section 170.

enforcement of the Act. However, it is possible that the last part of the provision stating that the notices may only be issued if the alleged contravention could otherwise be addressed by an application to court or to the Companies Tribunal, may substantially limit the scope of the provision.

The remedial and enforcement provisions of the Companies Act of 2008 are set out in chapter 7 of the Act, as read with the regulations in chapter 7 of the Companies Regulations. These provisions provide detailed steps and procedures in order to enforce compliance with the Act and the regulations. Section 157(1) of the Companies Act 2008, provides the Panel with extended authority to apply to court in any matter that is ; (a) directly contemplated in the particular provision of this Act; (b) acting on behalf of a person contemplated in paragraph (a), who cannot act in their own name; (c) acting as a member of, or in the interest of, a group or class of affected persons, or an association acting in the interest of its members; or (d) acting in the public interest, with leave of the court.[405]

In addition, in terms of section 157(2) the Panel by itself (on its own motion according to the Act) and in its absolute discretion, may-

> "(a) commence any proceedings in a court in the name of a person who, when filing a complaint with the Commission or Panel, as the case may be, in respect of the matter giving rise to those proceedings, also made a written request that the Commission or Panel do so; or
> (b) apply for leave to intervene in any court proceedings arising in terms of this Act, in order to represent any interest that would not otherwise be adequately represented in those proceedings."

The Panel will play a central role in complaints concerning contraventions of the affected transaction provisions in Chapter 5 Part B and C. In terms of section 168, any person may lodge a complaint with the Panel or the Panel may

[405]Section 157(1) of the Companies Act of 2008.

initiate a complaint[406] or the Minister may direct the Panel to investigate.[407] The Panel must investigate in terms of a directive from the Minister,[408] but may in other cases: refuse to investigate in some cases;[409] refer the matter to the Companies Tribunal or an accredited entity that could attempt alternative dispute resolution (which would probably seldom occur in respect of the Panel as it would seem that this alternative is intended for the Commission); or appoint an inspector or investigator to investigate the complaint in terms of section 169(1)(c).[410] During the investigation, the Panel may designate a person or persons to assist the inspector or investigator. In appropriate cases, the Panel may request a company for a joint appointment with the company of an independent investigator, at the expense of the company or on a cost sharing basis, to report to it, the Commission and the company.[411] The Panel may also apply to court for appointment of an independent investigator at the expense of the company, to report to it, and the company.[412] The Commission or Tribunal may furthermore refer any complaint to the Panel in terms of section 170(1)(b), if the Panel is the authority that should deal with it.[413]

In order to encourage co-operation during investigations, the Panel may issue summons. In the summons, it may request persons to appear, produce or deliver specified documents. Persons so summoned are entitled to protection against self-incrimination.[414] On conclusion of the investigation, if the Panel chose to investigate, it may among other things: excuse the person against whom a complaint has been raised,[415] refer the matter to the Tribunal, the Commission or the Panel, if the matter falls within their jurisdictions,[416] refer the matter to the National Prosecuting Authority,[417] or another authority when it

[406]See section 168(1) and 168(2) of the Companies Act of 2008 read with regulation 135.
[407]Section 168(3) of the Companies Act of 2008.
[408]Section 169(1) of the Companies Act of 2008.
[409]See regulation 135(4).
[410]Section 169(1) of the Companies Act of 2008, read with regulation 137(1).
[411]Section 169(2)(b)(i), of the Companies Act of 2008.
[412]Section 169(2)(b)(ii), of the Companies Act of 2008.
[413]See the analysis of this provision below.
[414]Section 176 of the Companies Act of 2008. See also regulation 137.
[415]Section 170(1) (a), of the Companies Act of 2008.
[416]Section 170(1)(b) of the Companies Act of 2008 read with regulation 140(1).
[417]Section 170(1) (f). of the Companies Act of 2008

believes that an offence or other legislative contravention has been committed,[418] issue a notice of non-referral to the complainant,[419] initiate legal proceedings in the name of the complainant in appropriate cases,[420] or issue a compliance notice.[421] The decision of the Panel after the investigation may be published.[422] Such a compliance notice may require a person to restore the assets to a company or to any other person or cease or correct or reverse any action that is in contravention of the Companies Act of 2008. A person who has been issued with such a notice may object by application to the court or the Takeover Special Committee (TSC) in terms of section 172 and follow a procedure set out therein, including making representations.[423] In terms of section 172(4), a decision by the TSC is binding, subject to a right of review or appeal to a court.

The compliance notice issued by the Panel remains in force until it has been set aside upon review by the TSC, or a court. Furthermore, a decision of the TSC can be taken on review by a court, while a decision by a court may be reviewed or appealed.[424] The Executive Director may issue a compliance certificate once compliance has been achieved.[425] When a compliance notice is issued to a person, a copy of such a notice must also be sent to any licensing authority that granted the licence authorising that person to conduct business.[426] It appears that this provision is intended to ensure that professional bodies are aware of the conduct of professionals they have registered and granted licences to. For instance, it is common practice that the independent expert report is issued by a chartered accountant, and if it is found that there is a contravention of the Takeover Provisions after an investigation, such a professional may be reported to the relevant professional body. Similarly, should any professional provide misleading information during a takeover or merger, she/he may be reported to the relevant body. This provision may deter

[418]Section 170(1) of the Companies Act of 2008.
[419]Section 170(1)(c) of the Companies Act of 2008 read with regulation 140(2).
[420]Sections 157(2) and 170(1) (e) of the Companies Act of 2008.
[421]Section 171(1) of the Companies Act of 2008.
[422]Section 170(2) of the Companies Act of 2008.
[423]Sections 172(1) and 172(2) of the Companies Act of 2008.
[424]Section 171(5) and 172 of the Companies Act of 2008.
[425]Section 171(6) of the Companies Act of 2008 read with regulation 139.
[426]Section 171(3) of the Companies Act of 2008.

potential transgressors from contravening the Companies Act of 2008 as it may have a negative effect on the conditions of their licence or professional standing.

In terms of section 171(7), failure to comply with a compliance notice issued may result in a person being fined up to 10 percent of the company's annual turnover or a maximum of R1 million by a court on application by the Panel, or a referral to the National Prosecuting Authority for prosecution as an offence, but not both. Perhaps the legislature should have ensured that the decisions of the TSC are capable of enforcement in a similar manner as those of the Appeal Board of the Financial Services Board (Appeal Board) that first came into existence under section 26 of the Financial Services Board Act 97 of 1990.[427] The form of the Appeal Board was subsequently expanded and its procedures amended under the Financial Services Laws General Amendment Act No 22 of 2008. Section 26A and 26B dealt with the Appeal Board, its panels and appeals proceedings. The Appeal Board has since been replaced by the Financial Services Tribunal (Tribunal) established under section 219 of the Financial Sector Regulation Act 9 of 2017 (FSR Act).The Tribunal under the FSR Act may have as many members as decided by the Minister of Finance, but must have at least two retired judges or persons with suitable experience in law and, at least two other persons who have experience or expert knowledge in financial services, financial products, financial instruments, market infrastructures or the financial system.[428] Under section 235 of the FSR Act, the decisions of the Tribunal may be taken on judicial review in terms of the Promotion of Administrative Justice Act 3 of 2000, or any other applicable law. Where an order issued by the Tribunal has not been taken on review within the time period set, or the proceedings for review have been completed, a party to the proceedings may file a certified copy of the order made by the Tribunal with the registrar of a competent court.[429] On being filed, the order of the Tribunal

[427]See Financial Services Conduct Authority "General Information" available at: https://www/fsca.co.za/Enforcement-Matters/Pages/About-FSB-Appeal-Board.aspx. (Accessed 2 -6-2018).
[428]See section 220(1)-(2) of FSR Act.
[429]Section 236(1) of the FSR Act.

has effect of a civil judgment and may be enforced as if given in that court.[430] This facilitates quick and efficient enforcement of the Tribunal's decisions. Had the TSC had similar enforcement provisions, its decisions would then have been civil court judgments capable of enforcement as such. This would have facilitated speedy enforcement of the decisions of the TSC.

In addition to creating offences specifically relating to failure to comply with compliance notices in the context of affected transactions and offers, a number of sections are aimed at ensuring that the Panel is able to perform its functions and investigate transgressions without being obstructed by the parties. These provisions include section 213 relating to breach of confidence, section 214 dealing with the making of false statements, reckless conduct and non-compliance, and section 215 relating to any actions intended to hinder the Panel in administering the Companies Act of 2008. The maximum period of imprisonment for convictions for any offences in terms of sections 213 and 214 is 10 years, or a fine, or both.[431] In the case of other offences a person may be imprisoned for a period of no more than 12 months.[432] However, a person may not be subject to both an administrative fine and imprisonment in the case of non-compliance under the same compliance notice.[433] It is suggested that the legislature considers contraventions of section 213 and 214 to be more serious, hence the higher penalties as compared to offences in terms of other sections.[434]

Any person may commence a civil action against any other person for loss or damage suffered by that person as a result of any contravention by such a person of any provision of the Companies Act of 2008.[435] This section is similar to section 440M (4) of the Companies Act of 1973. The Panel may also apply to court to declare a director to be a delinquent or under probation in certain

[430]Section 236(2) of the FSR Act.
[431]Section 216(a) of the Companies Act of 2008.
[432]Section 216(b) of the Companies Act of 2008.
[433]Section 171(7) of the Companies Act of 2008.
[434]See sections 216 of the Companies Act of 2008.
[435]Section 218 of the Companies Act of 2008.

circumstances,[436] for instance where the director has been acting as a director contrary to the provisions of section 69, due to the disqualifications in that section, or if he has abused his position as director.[437] The Act gives *locus standi* to a broad range of persons and such declarations have serious implications for directors, including automatic removal as directors.[438] In one of the first cases of this nature under the Act,[439] an unreported case of *Kukama v Lobelo,*[440] the court declared a director delinquent due to a number of transgressions by the director, which included: gross negligence by failing to detect tax fraud.[441] Other instances that could lead to a declaration of delinquency by courts include: gross abuse of position as director; and taking personal advantage of information or opportunity belonging to the company.[442]

In order to assist and strengthen investigations into alleged non-compliance with the provisions of the Companies Act of 2008, section 159(4) offers whistle-blowers protection from any civil or criminal liability for disclosures made, subject to certain safeguards.

The Companies Act of 2008 also includes an anti-voidance, exemptions and substantial compliance provision in section 6. A quick overview of the section suggests that it is intended to strengthen the provisions of the Act, promote accessibility, provide flexibility in application of the Act and also reduce technical arguments about compliant or non-compliant documents or procedures. In terms of the section, the Panel, the Commission or an exchange in respect of a listed company on that exchange, may apply to court to declare any agreement, transaction, resolution, arrangement or provisions of an MOI or rules: (a) to be substantially or primarily aimed at defeating or reducing the effect of a prohibition or requirement established by or in terms of the

[436]Section 162(3) of the Companies Act of 2008.
[437]Section 162(5) of the Companies Act of 2008.
[438]R Cassim "Delinquent directors under the Companies Act 71 of 2008" (Jan/Feb 2013): 26 *De Rebus* 14.
[439]Cassim (Jan Feb 2013) *De Rebus*)14.
[440]South Gauteng High Court, Case No 38587/2011.
[441]Delport *Henochsberg on the Companies Act 71 of 2008* 566.
[442]566.

unalterable provision of the Act; and (b) void to the extent that it defeats or reduces the effect of a prohibition or requirement established by or in terms of an unalterable provision of this Act.[443] In appropriate cases, the Companies Tribunal, on application by any person may issue an administrative order exempting an agreement, transaction, resolution, arrangement or provisions of an MOI or rules from any prohibition or requirement established by or in terms of an unalterable provision of the Act, except in the case of a provision that falls within the jurisdiction of the Panel.[444] Accessibility and flexibility in the application of the Act comes in a number of ways. For instance, accessibility can be found in use of plain language,[445] or allowing documents to be transmitted in electronic form.[446] Flexibility is applied by: allowing unaltered electronically or mechanically reproduced documents, except share certificates;[447] allows for usage of additional filing methods in addition to those prescribed in the Act;[448] acceptance of prescribed forms, notice or documents as sufficient, if they satisfy all the substantial requirements.[449] Further, deviations from a designated document or content, are allowed, provided that the deviations do not negatively and materially affect the substance of the document, record, statement or notice; or would reasonably mislead a person reading the document, record, statement or notice.[450]

5 9 An overview of the takeover regulations and the information required

The Minister, in consultation with the chairperson of the Panel and by notice in the Gazette, may prescribe regulations in respect of affected transactions and offers.[451] This is similar to the Companies Act of 1973 where the SRP made

[443]Section 6(1) of the Companies Act of 2008.
[444]Section 6 (2) of the Companies Act of 2008.
[445]Section 6(5) of the Companies Act of 2008.
[446]Section 6(10) of the Companies Act of 2008.
[447]Section 6(7)) of the Companies Act of 2008.
[448]Section 6(14) of the Companies Act of 2008.
[449]Section 6(8)(a) of the Companies Act of 2008.
[450]Section 6(8)(b) of the Companies Act of 2008.
[451]Section 120 of the Companies Act of 2008.

rules, which were then approved by the Minister.[452] Under the Companies Act of 1973 this led to the creation of the SRP and SRP Code.

Under the Companies Act of 2008, the regulations that govern takeovers and mergers no longer form a separate code. Some of the rules of the SRP Code are now in the Takeover Regulations, while others are in chapter 5 of the Companies Act of 2008. Some of the general principles of the SRP Code[453] have now become part of the Companies Act of 2008.[454] A quick overview of the Takeover Regulations shows that they were written on an assumption that offerors would use a general offer as a main means of undertaking a takeover or a merger, even though the regulations apply to all affected transactions.[455] This is not surprising because the SRP Code on which they are mostly based was similarly premised.[456]

The Takeover Regulations mainly deals with procedures, information and disclosures required to ensure compliance with chapter 5, Part B and C of the Act. The Takeover Regulations provide detailed requirements with which offerors and offeree regulated companies must comply in order to ensure that the principles set out in, among others, section 119(1) and section 119(2) of the Companies Act of 2008 are complied with. For instance, the principles in section 119(1)(a) are given effect in regulations 111(4) and 111(5), which require that bidders provide bank guarantees or confirmations that they have cash to complete the transactions. The regulations are aimed at upholding various principles, such as, maintaining the integrity of the market as stated in section 119(1)(a). Parties must also be able to pay and comply with the various Takeover Provisions, so as to avoid failed takeovers or mergers.

Regulation 117 requires that the Panel must approve all documents relating to takeovers or mergers prior to publication or posting to shareholders. The documents include announcements and circulars relating to affected

[452]Section 440C of the Companies Act of 1973.
[453]See General Principles 1 to 11 of the SRP Code.
[454]See Luiz (2014) *Merc LJ* 563.
[455]561.
[456]See SRP Code.

transactions. This is an important tool for ensuring the provision of accurate and relevant information in the context of affected transactions and in a timely manner. The Takeover Regulations support the disclosure and transparency in respect of takeovers and mergers. They also ensure that equality and fairness principles for shareholders of regulated companies are adhered to. The regulations provide for a detailed and orderly takeover or merger process, from the beginning to the end of a takeover or merger.[457] For instance, regulation 106, dealing with a circular to securities holders, provides detailed requirements concerning the information to be sent to shareholders. A closer look at regulation 106 shows that it is one of the important regulations as it provides the most comprehensive disclosure requirements by both the offeror and the offeree regulated company.

In addition, section 114(2) of the Companies Act of 2008, read with regulation 90, requires companies undertaking these transactions to retain an independent expert to advise the independent board of the offeree company or offeror in some cases.[458] The independent board must provide the report about the offer to the relevant securities holders and also express their opinions about the offer. This is to provide some guidance to shareholders and assist them in making an informed decision.[459] In order to ensure that securities holders are given enough time to consider the merits or demerits of an offer and have sufficient time to obtain advice, if they so wish, the regulations set out various timelines within which transactions must be undertaken and also provide how long offers should be open for acceptance by shareholders.[460]

However, the information disclosed in circulars about certain affected transactions may be of limited use to shareholders due to inclusion of unnecessary information. Perhaps section 121 of the Companies Act of 2008 and the Takeover Regulations should set limitations on the type, length of document, and manner in which information must be disclosed. Circulars to

[457]See regulations 99 to 106.
[458]See regulation 110(10) (a).
[459]See regulation 110.
[460]Luiz (2014) *SA Merc LJ* 565.

shareholders are often long and complex. There is a risk that important information can be buried in the circular.[461] It is also doubtful whether the addition of more disclosures will necessarily assist shareholders in making an informed decision. Complicated and long documents may discourage shareholders from reading the contents of the circulars in their entirety. Shareholders are likely to follow the course of action proposed by companies and their advisers.[462] These proposed actions are usually placed prominently at the beginning of the circular.[463] The circulars are often written in hyperbolic language intended to persuade shareholders to support a takeover or merger. Researchers have commented about circulars as follows:

> "[O]ne of its purposes is to induce shareholders to accept the offer or vote in favour of the proposed resolutions; one must also expect to find an element of salesmanship."[464] It is suggested that a simplified document could be sent to shareholders written in simple understandable language to accompany the detailed circulars which complies with the Act and the regulation."[465]

Only information that is relevant to the current affected transactions should be published or included in the announcement or circular. Other transactions that may require approval by shareholders, but do not relate to the current takeover or merger should be excluded. Circulars dealing with affected transactions should not be used for any other purpose. Regulations could also require all such documents and announcements to be written in plain language.[466] This may assist shareholders in focusing on the relevant information, and ultimately making better decisions about a takeover or merger. Further, there should be limitations on the amount of information contained in circulars and avoid

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[461]See among others, circular to the shareholders of Steinhoff International Holdings Limited relating to the scheme of arrangement dated 7 August 2015.

[462]The proposed actions include attendance of the meeting, when will a transaction become effective. The latter implies how long it will take for shareholders be paid.

[463]See Circular to Murray & Roberts Holdings Limited shareholders dated 9 April 2018 "Action required" on first page.

[464]Macgregor (1978) *S African LJ* 329 -338.

[465]339.

[466]The SEC has published a handbook for general information only, on techniques for writing in plain English to create clearer and more informative disclosure documents. See SEC "A Plain English Handbook: How to create clear disclosure documents" 1998. Available https://www.sec.gov/pdf/handbook.pdf.(Accessed 1-12-2016).

unnecessary verbiage. There should be an emphasis on the quality of information provided to shareholders rather than quantity.

The current Takeover Regulations should be seen as a working document due to some glaring inaccuracies. It has been argued that the validity of certain regulations can be challenged on the basis that, as subordinate provisions, they are *ultra vires* to the principal provisions in the Act as some of them go beyond their empowering sections. It is suggested that practitioners have learnt to work around the provisions and make them practically workable. For example, it is common practice for practitioners to treat share repurchase transactions in terms of section 48(8)(b) as affected transactions and obtain approval or an exemption from the Panel before such transactions are implemented.[467] Latsky asserts that a consensus is emerging among practitioners as to how to work around ambiguities.[468] Nevertheless, this remains unsatisfactory. Regulations should be clear to foster certainty and encourage compliance. This will also make it easy for regulators to enforce, and create certainty for offerors and offeree regulated companies about their obligations to comply.

5 10 An overview of the Panel's general power to exempt affected transactions

The Panel may grant exemptions to offerors or affected transactions in terms of section 119(6) of the Companies Act of 2008. The power to grant exemptions in section 119(6) is even wider than the SRP's equivalent powers in terms of the Companies Act of 1973.[469] The drafters wanted to achieve flexibility and to avoid unnecessary compliance.[470] In terms of the section, the Panel may wholly or partially exempt application of any of the provisions relating to takeovers and mergers or the regulations with or without conditions. The exemption may be granted if: (a) there is no reasonable potential for prejudicing the interests of

[467]See among other circulars, Basil Read Holding Limited Circular dated 2 November 2017 on page 26.
[468]Latsky (2014) *Stell LR* 362.
[469]Boardman (2010) *Acta Juridica* 319.
[470]319

any party to the transaction;[471] (b) the cost of enforcing compliance will be disproportionate to the transaction;[472] or (c) the exemption is reasonable and justifiable in the circumstances, taking into consideration the principles and purposes of the Takeover Regulations.[473] The SRP had powers to grant exemptions from compliance with the SRP Code in broad terms in terms of Rule 34.[474] The ability of the Panel to grant exemptions in terms of this section is narrowly circumscribed, because the Companies Act of 2008 sets out a number of factors that the Panel must consider before granting the exemption. It is possible that section 119(6)(c) could be interpreted in such a way that it could afford wide grounds for exemption. This is so considering that the other two requirements relating to prejudice[475] and cost of compliance[476] are limiting. The issue of reasonableness and justifiability does not appear to be as limiting as the other two provided that some basis has been established for such a conclusion. It has been indicated that section 119(6)(c) exemption is broad and all encompassing.[477]

The Panel does not have authority to regulate affected transactions relating to fundamental transactions entered into by a company that is subject to an approved business rescue plan in terms of Chapter 6 of the Companies Act of 2008.[478] The discussions and the issues as to whether the Panel should also regulate such transactions are complex and outside the scope of this dissertation.

[471] Section 119(6) (a) of the Companies Act of 2008.
[472] Section 119(6) (b) of the Companies Act of 2008.
[473] Section 199(6) (c) of the Companies Act of 2008.
[474]See rule 34 of the SRP Code, which provided in general terms that the Panel shall enjoy a general discretion to authorize, subject to such terms and conditions as it may prescribe, non-compliance with or departure from any requirement of the Code and to excuse or exonerate any party from failure to comply with any such requirement.
[475]Section 119(6)(a) of the Companies Act of 2008.
[476]Section 119(6)(b) of the Companies Act of 2008.
[477]See Boardman (2010) *Acta Juridica* 319.
[478]Section 118(3) of the Companies Act 2008.

5 11 Concluding remarks

From the analysis in this chapter, it is suggested that the intention of the legislature of promoting transparency, certainty and efficiency in respect of the SA takeover and merger regime has been achieved to some extent. The provisions on affected transactions also ensure that the South African takeover regulation is kept up to date with the best international merger and takeover practices as was envisaged in the DTI 2004 Policy document.[479] With increasing globalization and resultant cross-border takeovers and mergers, new regulations may encourage inward investment and increased takeover and merger activity in South Africa. Further, the updated regulations encourage development of a market for corporate control as the rules of takeover and merger are clearer. Investors and market participants will have confidence in South African corporate law. It has been indicated that the Company Act 2008 is “world-class” and puts South Africa in the forefront of corporate law reform.[480] However, it is argued that certain parts of the legislation need improvement. In particular, some of the Takeover Provisions need attention.

Similar to takeover rules in other countries, the Takeover Provisions seek to maintain integrity of the markets, ensure fairness and equity to shareholders. The takeover procedures are aimed at protecting shareholders during takeovers or mergers, no matter which method is used. This is achieved by requiring that affected transactions must disclose sufficient information in a timely manner. Pressure tactics and preferential treatment is prohibited. The Takeover Provisions create a system of regulation that assures protections of shareholders beyond the mandatory offer requirements.

It is at arguable that the framework of protection provided by the Takeover Provisions provide better protection to shareholders than under the 1973 Act and the previous SRP Code. Inter alia it may be mentioned that:[481] the

[479]DTI 2004 Policy document.
[480]MM Katz “Governance under the Companies Act 71 of 2008: Flexibility is the keyword” 2010 *Acta Juridica* 262.
[481]The aspects in this list are in addition to other protective measures mentioned elsewhere in this part.

definitions of affected transactions in the 2008 are clearer, the powers of the TRP to regulate affected transactions have been enhanced and they are clearly set out in the Act, the Takeover Regulations are written in the style of peremptory rules and the less formal and more general style of the SRP Code has been abandoned,[482], the requirement for independent experts has been strengthened in section 114(2), read with regulation 90, which deals with fairness opinions and valuations during affected transactions, and regulation 106(11) which sets out a clear requirements that documents must to be available for inspection by shareholders.

The Companies Act of 2008 attempts to attain a balance between minority protection and giving effect to the will of majority shareholders. Minority shareholders may not obstruct an affected transaction but are afforded protection by among others: disclosures, voting, appraisal rights, dispute resolution procedures and enforcement measures. The important protections for shareholders in terms of the Companies Act of 2008 are the shareholder approval, court review in certain circumstances, and the shareholder-appraisal remedy.[483] The legislature has, in general, retained most of the provisions of the Companies Act of 1973 in respect of regulating takeovers and mergers. The new provisions seem to be in line with what was intended in the DTI 2004 Policy document. In general, the new takeover and merger provisions have been welcomed and are regarded as an improvement on the Companies Act of 1973 and the SRP Code. However, it may take some time before the efficacy of the new provisions can be properly determined. Moreover, some sections and regulations need to be amended, for simplicity and clarity.

However, while the Takeover Provisions have been welcomed and commended, there are a number of flaws in both the substantive provisions and in the regulations. These make it difficult to interpret and apply them and should be attended to as quickly as possible for the benefit of shareholders.

[482]See SRP Code.
[483]Davids *et al* (2010) *Acta Juridica* 337-338.355.

These include:

(a) Formulation resulting in a poor relationship between the Act and the regulations. For example, section 125 of the Companies Act of 2008 and regulation 88, relating to comparable and partial offers. As indicated in paragraph 5 6 11 the provisions are very difficult to follow.

(b) The mandatory offer requirements as critically discussed under paragraph 5 6 9 above.

(c) Complex and lengthy procedural requirements relating to appraisal rights as discussed under paragraph 5 6 6 above.

(d) Other provisions that must be improved including: (i) the overreaching section 118(1)(c)(ii), which makes the Takeover Provisions applicable to small, private companies discussed under paragraph 5 5 above. As indicated, compliance with the requirements are costly for private companies; (ii) section 48(8)(b) discussed under paragraph 5 6 5 above, (iii) section 122 relating to disclosures as indicated under paragraph 5 6 7 above; and (iv) the inefficient remedies and enforcement mechanisms as discussed under paragraph 5 8.

In addition, the division of chapter 5 into part A, B and C, limits the authority of the SA Panel only to fundamental transactions that constitute affected transactions.[484] The SA Panel is not able to regulate or provide exemption, as indicated by Latsky, in the cases of fundamental transactions that are not affected transactions.[485] The SA Panel will not be able to grant exemptions from the application of the provisions regarding fundamental transactions in Chapter 5 Part A, although they are an inherent part of many fundamental transactions. Where fundamental transactions are not affected transactions, the SA Panel will have no power to regulate transactions including granting any exemptions from overly-strict rules regarding fundamental transactions. In particular, closely-held private companies may not apply to the SA Panel for an exemption not to comply with certain requirements regarding fundamental transactions. It

[484]See Latsky (2014) *Stell LR* 378.
[485]370.

is not clear from the Act if such companies may apply to the Companies Tribunal for such relief. This is inappropriate and the SA Panel should have powers to regulate all transactions falling under chapter 5, and not only those under part B. The enforcement and remedies of the SA Panel should be simplified and strengthened as discussed under paragraph 5 8. Adopting the enforcement mechanism similar to that of the Financial Services Tribunal created under section 219 of the Financial Sector Regulation Act 9 of 2017, will make the process of enforcement effective and efficient. As discussed under paragraph 5 9, the information and procedures could be improved such that the quality of the information provided is improved to enable shareholders to make informed decisions rather than quantity, which may impede and prevent shareholders from getting the relevant information. Some of the shortcomings of the various Takeover Regulations have already been identified under paragraph 5 10 and these should also be rectified.

Chapter 6: Evaluating takeover and merger provisions of the selected countries

"The classical assessment of the mandatory bid rule by law and economics scholars is rather negative."[1]

6 1 Introduction

This chapter evaluates regulation of takeovers and mergers in the comparative countries as discussed in chapter 2 in the case of the US, chapter 3 in the case of the UK, chapter 4 in the case of Australia and chapter 5 in the case of SA. The evaluations include the companies and types of affected transactions regulated, authorities regulating the transactions, dispute-resolution procedures and enforcement measures relating to affected transactions. Arguments for and against the mandatory offer rule are also evaluated. Takeover regulators are concerned with the possibility that mergers and takeovers may negatively impact the interests of various stakeholders of the company. Fraud, misleading information and poor disclosures, among others, were the main motivating factors for countries to develop stronger regulations for takeovers and mergers. In order to discourage and reduce the potential harm to shareholders, countries have adopted different methods to regulate takeovers and mergers. Mayer[2] puts it as follows:

> "There is no greater source of regulation than scandals. Regulatory inaction in the face of fraud or deception is impossible."[3]

The review suggests that the SA takeover and merger regulations and procedures are closely related to and similar to that of the UK. However, the US and Australian takeover and merger regulatory procedures are different

[1]EP Schuster "Efficiency in Private Sales -The Case for Mandatory Offer Bids" (2010) *LSE Law, Society an Economy Working Papers 08/2010 London School of Economics and Political Science* 3.
[2]C Mayer "Corporate Governance: A Policy for Europe" (2003) *A Paper presented at Saïd Business School, University of Oxford.* This paper was presented at the 2003 Annual Congress of the Swiss Society of Economics and Statistics at the University of Bern on 21 March 2003.
[3]Mayer (2003) *Saïd Business School, University of Oxford*.

from those of UK and SA. Accordingly, the evaluation will concentrate on the takeover and merger provisions of the UK and SA. Where applicable, the US and Australian takeover and merger regulatory environment will be referred to.

6 2 A brief evaluation of developments of regulation of takeovers and mergers in the selected countries

The reasons for regulation of takeovers and mergers by countries are similar. These include protection of investors and promoting investor confidence. Presumably, countries would select the preferred regulatory authority based on a number of aspects, including efficiencies and effectiveness of the type of regulatory model. The development of SA takeover and merger laws were closely influenced by those of the UK. However, it is generally accepted that the UK and the US have similar economic markets, including their levels of development, and similar-sized companies.[4] Yet despite these similarities, their takeover methods are markedly different. Australia, even though it has historical and economic connections with the UK, has adopted a completely different method of regulating takeovers and mergers. Australian company law started off with the transplantation of UK company law. However, its company law has since evolved to suit local conditions. It is suggested that Australia recognised that the law had to be responsive to economic development of the country.[5] According to Amour and Skeel Jr,[6] the content of takeover rules has been influenced fundamentally by differences in the manner in which takeovers and mergers are regulated in the UK and the US. In the UK, the initial self-regulation of takeovers has led to a regime, which is mostly driven by the interests of institutional investors, whereas in the US, the dynamics of judicial lawmaking, mostly by the Delaware judges, benefit directors by making it

[4]See JA Armour & DA Skeel Jr "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of US and UK Takeover Regulation" (2007) 95 *Georgetown Law Journal* 1727, and J Franks, M Mayer & S Rossi "Spending Less Time with the Family: The Decline of Family Ownership in the United Kingdom" in Morck (ed) A History of Corporate Governance around the World: Family Business Groups to Professional Managers (2005) 584, among other scholars who agree to this view.
[5]See P Lipton "History of Company Law in Colonial Australia: Economic Development and Legal Evolution" (2007) *31 Melbourne University Law Review.* 806.
[6]See Armour & Skeel Jr (2007) *The Georgetown Law Journal* 1764-1765.

relatively difficult for shareholders to influence the rules.[7] One of the first hostile takeovers in the UK occurred during 1953 with the acquisition of J. Sears Holdings Limited. Franks *et al*[8] suggest that this takeover introduced the concept of paying a premium to shareholders. It appears that for a short period in the UK, during the 1950s and 1960s, there was an unregulated takeover market. This created a potential for parties to acquire control by discriminatory means. Partial offers were also used to acquire effective control due to the fact that hostile takeovers were seen as increasing the costs of a full takeover bid.[9]

As discussed in Chapter 3, the UK Panel was established during 1968. Two of the first rules enforced by the panel through the UK City Code were the equality rule and the mandatory offer rule. These two rules had the effect of increasing shareholder concentration and preventing discriminatory offer prices.[10] The market for corporate control developed further during the 1970s, with a larger body of institutional shareholders, wider protection for minority shareholders and an active market for hostile offers.[11] Until a few years ago, the UK City Code was not based on statute and was self-regulatory. The introduction of the EU Directive and the UK Companies Act 2006 changed this position.[12] However, it was asserted that, despite its statutory nature, the UK City Code should be regarded as self-regulatory.[13]

Australia's takeover and merger provisions are based on the main Eggleston Principles.[14] These principles form the cornerstone of section 602 of the Australian Corporations Act 2001. The provisions of the Act are enforced by

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[7]Armour & Skeel Jr (2007) *The Georgetown Law Journal* 1764-1765.
[8]Franks *et al*, "Spending Less Time with the Family: The Decline of Family Ownership in the United Kingdom" in *A History of Corporate Governance around the World: Family Business Groups to Professional Managers* 584.
[9]584.
[10]585.
[11]585.
[12]See Chapter 1 of Part 28 of the UK Companies Act 2006 (as amended by The Companies Act 2006 (Amendment of Schedule 2) (No 2) Order 2009). Rules are set out in the Takeovers Code (including this Introduction, the General Principles, the Definitions and the Rules (and the related Notes and Appendices).
[13]A Johnston "Takeover Regulation: Historical and Theoretical perspectives on the City Code" *Cambridge Law Journal* (2007) 66:2, 447.
[14]Section 602 also incorporate additional principles relating to efficient, competitive and informed market as well as compulsory acquisitions. See guidance note 1 at paras 30-31.

two bodies, namely, ASIC and the Australian Panel.[15] The UK and SA takeover legislation has similar mandatory offer provisions, while Australia has adopted unique takeover principles.[16] In Australia, there is a prohibition against acquisitions of 20 percent voting securities, unless certain requirements are met.[17] The reasons for developing takeover laws in Australia were to prevent potential prejudice to shareholders during takeovers.[18]

According to researchers, most UK companies have dispersed shareholding structures.[19] It has been argued that the prevalence of dispersed or concentrated ownership resulted from the type of protection that existed in a particular country.[20] However, this is not necessarily the case due to the fact that strong investor protection took some time to be accepted by market participants and when it was accepted, substantial dispersed ownership had already taken root.[21] This seems to support a view that it was not strong regulatory measures that led to dispersed ownership. It is suggested that introduction of strong protective measures was motivated by various stakeholders, such as financial firms and stock exchanges that desired to build a good reputation with investors.[22] Shareholder dispersal in the US occurred sometime during the 1930s, while the dating of dispersed shareholdings in the UK is not well established.[23]

The UK City Code brought improved compliance through the supervision of takeovers by the UK Panel and allowed the UK Panel to force compliance on its constituencies. This was done by "piggybacking" on the London Stock

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[15]See discussions under paragraph 4 2 3 in Chapter 4 dealing with Australian takeover and merger regulators.
[16]E Hutson "Australia's takeover rules: how good are they?" (2002) *Corporate Regulation,* Jassa Issue 4 Summer 33.
[17]Section 606 of the Australian Corporations Act 2001.
[18]Lipton (2007) *Melbourne University Law Review* 830. See also M Hoyle "An Overview of the Role and Powers of the Takeovers Panel" in Ramsay (ed) *The Takeovers Panel and Takeover Regulation in Australia* (2010) 39.
[19]See CM Bruner "Power and Purpose in the "Anglo-American" Corporation" (2010) 50:3 *Virginia Journal of International Law* 613.
[20]613.
[21]613.
[22]613.
[23]515.

Exchange's enforcement machinery. This was partly due to the fact that the London Stock Exchange had the ability to sanction listed companies.[24]

6 3 A brief evaluation of the authorities regulating takeovers and mergers in the selected countries

The research shows that there are a number of regulatory models. There are some differences and similarities in respect of how transactions are regulated in the comparative countries.

In Delaware the courts play an important role in enforcing the various corporate law rules, including those affecting applicable during takeovers and mergers.[25] The courts' roles are evident where conflicts involving directors that may negatively affect shareholders during a takeover or a merger continuously arise. Accordingly, the courts have developed some of the important principles dealing with conflicts of interests of directors during takeovers and mergers.[26] Unlike the other jurisdictions in this study no separate regulatory bodies plays an active role in enforcing takeover and merger rules and unlike South Africa and the UK, Delaware has no mandatory offer.

However, Delaware is an important comparator. It is perhaps the pre-eminent jurisdiction for merger law as most large US companies are incorporated there. The rules that apply to mergers in the other jurisdictions often have their origin in ideas that have emanated from Delaware even if they may have lost traction in that jurisdiction, such as the equal opportunity rule. Many of the rules regarding duties of directors will be relevant to the other jurisdictions under discussion even if they may have more expansive regulatory systems for mergers. The Delaware system like that of Australia furthermore shows that it is possible to properly protect shareholders without a mandatory offer rule. Finally, Delaware and its almost impenetrable case law perhaps also illustrates

[24] 627.
[25] See the discussions under paragraph 2 3 1.
[26] See discussions dealing with the standards of reviewing directors conduct during takeovers and mergers created by Delaware courts under paragraph 2 5.

why it may be better to put a more formal regulatory system for mergers in place. The ensuing comparison of institutions will accordingly concern the formal systems for merger regulation that exist in South Africa, the UK and Australia.

In the UK, shareholders of the offeree company have primary powers to decide on the merits of a takeover or a merger.[27] 'Decision rights' in respect of takeovers reside with shareholders.[28] The Australian regulatory regime has been described as restrictive.[29] Although its takeovers and mergers rules have similarities to other countries, it still has distinct features. In certain respects, the similarities are influenced by historical connections between the company laws of the countries. The UK, Australia and South Africa have dedicated authorities to regulate takeovers. However, each country has a different process for processing takeover documents.

In the UK, the City Code encourages parties to consult the Panel at an early stage of the transaction. Parties may consult the Panel to obtain informal advice on how the Panel would consider a proposed takeover or merger.[30] The UK Executive[31] may, inter alia: give opinions on application and effect of the UK City Code;[32] give rulings waiving certain requirements of the UK City Code,[33] and issue guidance in the form of published Practice Statements. The Practice Statements are non-binding.[34] The Companies Act of 2008 has similar provisions allowing the Panel to issue guidelines for the benefit of persons involved in affected transactions.[35] In South Africa, the Executive Director of

[27]See J Payne "Schemes of Arrangement, Takeovers and Minority Shareholder Protection" (2011) *II Part 1 Journal of Corporate Law Studies* 74.
[28]Franks et al in *A History of Corporate Governance around the World: Family Business Groups to Professional Managers* 585.
[29]See Hutson (2002) *Corporate Regulation, Jassa Issue 4 Summer* 33.
[30]See UK City Code in 6 of the Introduction.
[31]These are full-time employees of the Panel headed by the Director General.
[32]See UK City Code in 5 of the Introduction.
[33]See UK City Code in 6 of the Introduction.
[34]See the UK City Code in 6 of the Introduction.
[35]Section 201(2) (b)of the Companies Act of 2008.

the Panel may also provide non-binding opinions and binding rulings.[36] Unlike the UK and SA Panels, the Australian Panel may not issue advance rulings.[37]

The three systems can be distinguished when it comes to the question whether documents and circulars have to be pre-approved.

The Australian Panel does not review documents to be sent to shareholders as ASIC performs this function.[38] The Australian Panel is the primary adjudicator of disputes during takeovers and mergers, while ASIC administers the Australian Corporations Act 2001 (among other laws). In respect of takeovers and mergers, ASIC has powers to conduct investigations, monitor transactions, prosecute contraventions and develop policy.[39]

The UK Panel does not approve circulars or announcements to shareholders other than circulars containing a 'whitewash resolution' in terms of rule 9 of the City Code.[40] The UK Panel also does not review and pre-approve circulars prior to being sent to shareholders. The Panel expects parties involved in transactions to comply with the City Code as indicated under code responsibilities and obligations.[41] The City Code broadly provides which parties are responsible for compliance with the City Code and this includes not only directors of the companies involved in takeovers and mergers, but also their advisers.[42] The UK system by which parties are encouraged to consult with the Panel, and by which guidance can be given will assist parties where difficult issues regarding disclosures may arise.[43] However, no formal pre-approval of documents and circulars takes place in the UK. In the UK, practitioners must send copies of documents posted to shareholders to the UK Panel only for review at the same time as they are sent to shareholders. Should it be found that the circulars are deficient or not compliant with the UK City Code, the parties will be obliged to send revised circulars to shareholders.

[36]See regulation 118.
[37]Hoyle "An Overview of the Role and Powers of the Takeovers Panel" in *The Takeovers Panel and Takeover Regulation in Australia* 56.
[38]See the discussions in Chapters 4 2 3 above.
[39]See N Calleja *The New Takeovers Panel – A Better Way?* (2002) 2.
[40]See Appendix 1 to the UK City Code.
[41]See UK City Code in 3(f) of the Introduction.
[42]See UK City Code in 3(f) of the Introduction.
[43]See UK City Code in 3(f) of the Introduction.

Conversely, the South African Panel is required to review and pre-approve circulars to shareholders.[44] This is not appropriate and should be criticised. It is suggested that they may be misleading to shareholders. This is because a pre-approval process may create a wrong impression to shareholders that, since the Panel has vetted the documents, the Panel also approves that the merger or takeover is for the benefit of shareholders. This may mislead shareholders due to fact that Panel does not consider commercial advantages or disadvantages of takeovers or mergers.[45] The pre-approved circulars may give shareholders a false sense of comfort that a regulator agrees with the transaction. Even if shareholders may have wished to oppose an affected transaction or offer, they may not do so. It is suggested that the UK Panel does not pre-approve documents for a number of reasons, including, avoiding a wrong impression that a pre-approval means the panel agrees with the commercial advantages of the transaction and also to ensure that advisers and companies have greater responsibility in preparing the documents and do not rely on the vetting process by regulators.

According to the UK City Code, the Panel similarly does not consider financial advantages or disadvantages of takeovers and mergers as these are for the shareholders to decide.[46] In South Africa, as if to emphasise the importance of this provision, it is set-out in two sections, in sections 119(1) and 201(3) of the Companies Act of 2008. Contrary to takeover panels in UK and South Africa, the Australian Panel, in considering declaring circumstances unacceptable in respect of a takeover or a merger, may consider a broader range of matters, including reaction of the financial markets,[47] or how its decision is likely to be received by the investing community.[48] The Australian Panel's jurisdiction

[44]See section 119 (1) of the Companies Act of 2008 and the Takeover Regulations. Regulation 117 specifically states that the Panel must approve circular or announcement to shareholders.
[45]See sections 119(1) and 201(3) of the Companies Act of 2008. The sections confirm a similar approach adopted by the UK City Code.
[46]See UK City Code in 2 of the Introduction.
[47]See discussions on Australian Guidance Note 1 *Unacceptable Circumstances* in chapter 4 para 4 2 4.
[48]I Ramsay "The Takeovers Panel: A Review" in *The Takeovers Panel and Takeovers Regulation in Australia* 10-11.

extends beyond the parties involved in the proceedings.[49] Given the fact that the Australian Panel is tasked with interpreting and applying policies underlying the takeover provisions, rather than specific legal requirements, it is appropriate for it to look beyond a “strictly legal context”. Fairness and equity are also required.[50]

The SA Panel has powers to exempt transactions in section 119(6) of the Companies Act of 2008. The UK Panel has wide powers to derogate or grant waivers from application of its rules.[51] The SA exemptions are limited to those affected transactions or offers where there is no reasonable potential of the transaction prejudicing shareholders; if the cost of compliance is disproportionate relative to the value of the affected transaction or offer; or where giving the exemption is reasonable and justifiable in the circumstances of the transaction taking into consideration the principles and purposes of the Takeover Provisions.[52]

In Australia, ASIC have powers to exempt parties from compliance in terms of section 655A of the Corporations Act 2001. Prior to granting the exemption, ASIC must consider the principles set in section 602 the Corporations Act 2001.[53] However, there are notable differences between the Australian and the South African provisions and, the authorities that exercise powers to regulate takeovers and mergers. For example, in Australia, the powers to exempt transactions from compliance lies with ASIC, rather than the Australian Takeover Panel, but those powers are subject to review by the Australian Takeover Panel.[54] In South Africa, the Executive Director or Deputy Executive Director of the Panel may exercise powers to exempt [55] or the TSC where the

[49]E Armson “The Australian Takeovers Panel and unfair prejudice to third parties” (2004) *Australian Journal of Corporate Law* 204.
[50]192.
[51]See UK City Code 2(c) on Derogations and Waivers in Introduction.
[52]See section 119(6) of the Companies Act of 2008.
[53]These are the main principles for regulating takeovers and mergers.
[54]Ramsay “The Takeovers Panel: A Review” in *The Takeover Panel and Takeover Regulation in Australia* 8.
[55]Section 119(6) of the Companies Act of 2008 read with section 200(2) and 200(3) of the Companies Act of 2008.

matter has been referred to it.[56] Any decision by the Executive Director or Deputy Executive Director is subject to a review by the TSC.[57] The final arbiter in any dispute are the courts, as discussed under remedies and enforcement in chapter 5, paragraph 5 8 above.

6 4 A brief evaluation of the companies and types of takeover and merger transactions regulated in the selected countries

The US, generally does not have a mandatory offer rule, although no state is precluded from enacting such a rule.[58] However, the US disclosure regime similar to that required by section 122 of the 2008 Act, goes beyond those of the other jurisdictions.[59] Shareholders acquiring more than 5 percent must not only disclose their shareholdings, but also declare whether or not they are intending to effect a takeover or influence control and, if so, to provide detailed information regarding their plans and proposals.[60] The requirements are mainly aimed at revealing potential offerors at an early stage. In addition, the disclosures are aimed at wider issues of transparency.[61]

As pointed out, "[T]his is the corollary of there being no mandatory offer requirements under US federal law."[62] Boardman,[63] indicates that while the US may not have a mandatory offer bid, its disclosure rules aimed at flushing out potential bidders are aggressive. In addition, the board of directors has powers to frustrate a takeover bid should they believe that it is not in the interest of shareholders.[64] The measures offer protection to shareholders by empowering their board, rather than the shareholders. This would not be appropriate in the

[56]See section 202 (3)(a) of the Companies Act of 2008.
[57]Section 202 (3)(b) of the Companies Act of 2008.
[58]See discussion in paragraph 2 1 above, and also Boardman 2010 *Acta Juridica* 322 and 324.
[59]Boardman 2010 *Acta Juridica* 322.
[60]Boardman 2010 *Acta Juridica* 322.
[61]Boardman 2010 *Acta Juridica* 322.
[62]Boardman 2010 *Acta Juridica* 322.
[63]Boardman 2010 *Acta Juridica* 324 -325.
[64]See Boardman 2010 Acta Juridica 325. See also detailed discussions dealing with the standards of reviewing directors' powers set by the courts when considering defensive tactics under paragraph 2 5.

SA context, as the measure risks disenfranchising minority shareholders.[65]

The Takeover Provisions in South Africa apply to regulated companies as defined in section 117(1)(i), which includes public companies, state owned companies and private companies. However, in South Africa, section 118(1)(c) of the Companies Act of 2008 makes Takeover Provisions applicable to a wider number of private companies. The wide application of this section has been criticised by various commentators.[66] The South African takeover provisions are onerous to small privately-owned companies. The criticism against section 118(1)(c) of the Companies Act of 2008 has been discussed in chapter 5 above.

The UK City Code applies to all takeovers and mergers of companies listed on the stock exchange and certain private companies. The UK City Code applies to the following companies: private companies, if such private companies have had their securities admitted to trading on a regulated market or a multilateral trading facility in the UK or on any stock exchange in the Channel Islands or the Isle of Man at any time during the 10 years prior to the relevant date, or if dealings and/or prices at which persons were willing to deal in any of their securities have been published on a regular basis for a continuous period of at least six months in the 10 years prior to the relevant date, whether via a newspaper, an electronic price quotation system or otherwise; or if any of their securities have been subject to a marketing arrangement as described in section 693(3)(b) of the UK Companies Act at any time during the 10 years prior to the relevant date, or if they have filed a prospectus for the offer, admission to trading or issue of securities with the registrar of companies or any other relevant authority in the UK.[67]

The rules applicable to private companies in the UK appear to be intended to cover only private companies, which have widely held shares. It can be asserted that such requirements are necessary where companies have been

[65]Boardman 2010 *Acta Juridica* 325.
[66]PJ Sutherland "The State of Company Law in South Africa (A Review of Modern Company Law for a Competitive South African Economy by T Mongalo)" (2012) 1 *Stell* 157.
[67]See Introduction 3(a) of the UK City Code.

previously listed on an exchange or the companies' shares have been offered to the general public. This is due to the fact that where there is large number of shareholders involved, there is a greater chance of unfair and unequal treatment among them. Therefore, it is important that such shareholders be entitled to protection in terms of the takeover rules. Australia also appears to adopt a similar approach to the UK that only private companies that have a certain number of shareholders should be subject to takeover or merger provisions. The Australian takeover provisions apply to listed companies, unlisted companies that have 50 or more members and to listed managed investment schemes.[68]

Australia and the UK do not have the concept of treatment among them. Therefore, it is important that such shareholders be entitled to protection in terms of the takeover rules. Australia al extends to listed investment schemes.[69] The UK and South African takeover provisions, on the other hand, are limited to companies.[70]

The manner in which the transactions that are regulated are classified appears to differ from country to country although the type of transactions regulated are substantially the same. The SA Panel regulates affected transactions as defined in section 117(1) of the Companies Act 2008. These transactions have been dealt with in chapter 5 in this dissertation. The UK does not have a specified categorised list of transactions similar to South Africa. However, the UK City Code indicates that the transactions regulated are broadly referred to as 'takeover bids and 'merger transactions'. These transactions include schemes of arrangement. Other transactions include acquisitions by parent companies of shares in their subsidiaries, dual holding company transactions, new share issues, share capital re-organizations and offers to minority shareholders, which have as their objective or potential effect (directly or indirectly) obtaining or consolidating control of the relevant companies, as well

[68]See chapter 6 of the Australian Corporations Act 2001.
[69]Section 606 of Corporations Act 2001.
[70]UK City Code in 2 of the Introduction and in the case of SA, the definition of a regulated company in terms of section 117(1)(i) of the Companies Act of 2008.

as partial offers. These transactions are defined in broad terms as 'takeovers' and 'offers'.[71] Section 602 of the Australian Corporations Act 2001 provides for regulation of takeovers and mergers. Australian takeover provisions distinguish between market bids and off-market bids in section 616 of the Corporations Act 2001. The UK Companies Act 2006 and the UK City Code does not specify market bids or off-market bids. Similarly, SA has no such distinction.

The Australian takeover and merger procedures discussed in chapter 4 differs from those of the UK and South Africa in one very significant respect. Section 606 of the Australian Corporations Act 2001 has an outright prohibition to acquire or make an offer to acquire certain percentages of relevant interests in voting shares of specified companies. The starting point of the Australian takeover provisions is to prohibit specified acquisitions of voting shares or relevant interests in listed companies, in unlisted companies with more than 50 members, or in listed investment management schemes, unless the acquisitions have been exempted in terms of section 611 of the Corporations Act 2001.

The South African Takeover Provisions include disposals of the greater part or major assets or undertakings of companies in terms of section 112 of the Companies Act 2008, schemes of arrangements, mergers or amalgamations in addition to regulating transactions relating to acquisition of voting shares.[72] The South African takeover provisions, like those in the UK, empowers the Panel to regulate schemes of arrangement albeit that, the South African Act does not allow the Panel to regulate compliance with the Chapter 5 Part A that deals with the basic requirements for these transactions. Moreover, schemes of arrangement in South Africa will seldom involve the courts. This will be the case only where shareholders have requested the company to do so or have applied to the courts.[73] Voting procedures for schemes of arrangements in South Africa

[71] UK City Code in 3(b) of the Introduction.
[72] See definition of affected transactions in section 117(1) (c) of the Companies Act of 2008.
[73] Section 114 of the Companies Act of 2008. Schemes of arrangements are required to comply with the provisions of sections 114, 115 and 164 and the Takeover Regulations.

are similar to those in the UK.[74] In the UK, schemes of arrangement are subject to regulation by the UK Panel and the courts. The court process involves three steps.[75] An application must be made to court to convene a scheme meeting; shareholders must vote in favour of the scheme at the meeting and; an application must be submitted to court to sanction the scheme.[76] The court is not obliged to approve the scheme simply because shareholders have voted in favour of the scheme; it has an unfettered discretion to reject or approve it.[77] The documents presented to shareholders to enable them to vote at the scheme meeting must be in accordance with the UK City Code.[78] The UK Panel ensures that all the schemes of arrangement contain the disclosures as if they were offers made in terms of the rules contained in the UK City Code.[79]

In Australia, however, the Australian Takeover Panel has no powers to regulate schemes of arrangements. This is the exclusive domain of the courts. ASIC also reviews documents relating to a scheme and issues a statement indicating that it has no objection to the scheme. The statement is then presented at court.[80] However, researchers suggest that the supervisory role for schemes of arrangement must be shifted from the courts to the Australian Takeover Panel.[81]

Following a general offer or a mandatory offer, section 124(2) of the Companies Act of 2008 allows an offeror to acquire the shares of shareholders who have not responded to the offer where 90 percent of the shareholders to whom an offer was made, have accepted the offer in accordance with the section.[82] This is similar to the UK[83] and Australian[84] expropriation sections. Shareholders also

[74]See discussions in paragraph 5 6 4 in chapter 5 dealing with schemes of arrangement.
[75]Payne (2011) *Journal of Corporate Law Studies* 87.
[76]87.
[77]N Boardman "A critical analysis of the new South African takeover laws as proposed under the Companies Act 71 of 2008" (2010) *Acta Juridica* 316.
[78]See Appendix 7 to the UK City Code that deals with schemes of arrangements.
[79]See Appendix 7 to the UK City Code.
[80]See Boardman (2010) *Acta Juridica* 317.
[81]Hoyle "An Overview of the Role and Powers of the Takeovers Panel" in *The Takeovers Panel and Takeover Regulation in Australia* 26.
[82]See section 124 of the Companies Act of 2008 also referred to as "squeeze out".
[83]See UK Companies Act 2006, section 979(2) (a).
[84]See Chapter 6A of the Australian Corporations Act 2001.

have a corresponding right to force the acquirer who holds 90 percent to acquire their shares.[85] The squeeze out provisions give both the offeror and the shareholders of the offeree company, subject to compliance with its requirements, an opportunity to sell-out at the same initial offer price.[86] In the US, it appears that there is no federal law that provides for an explicit right for the remaining shareholders to compel the controlling shareholder to acquire their shares similar to section 124(4) of the Companies Act 2008. The DGCL also does not have a similar provision.[87] However, it is suggested that in certain instances freeze-outs and appraisal rights under section 262 of the DGL achieve similar results.

The UK has two thresholds for the mandatory offer to be triggered being 30 percent and 50 percent of the voting rights, as discussed in chapter 3 above, while SA has only one threshold of 35 percent. The mandatory offer in the UK must be subject to a condition that the offeror must receive acceptances which will result in it holding more than 50 percent of the voting rights. Further, the offeror must not trigger a mandatory offer if its implementation is subject to the passing of the offeror shareholders' resolution, other conditions, consents or arrangements.[88] SA has no such requirements. Another major difference between the Australian takeover provisions and those of the UK and South Africa is that the Australian takeover provisions do not have mandatory offer requirements as indicated in paragraph 4 2 2 of chapter 4 above.

A distinct feature of the South African Takeover Provisions as compared to those of UK and Australia is that fundamental transactions are subject to a requirement for appraisal rights in terms of section 164 of the Companies Act of 2008. The appraisal right remedy in terms of section 164 has been discussed in chapter 5 above. In this respect, South Africa follows the United States, in particular Delaware State. However, due to the different legal systems and

[85]See also Payne (2011) *Journal of Corporate Law* 72.
[86]See S Luiz "Protection of holders of securities in the offeree regulated company during affected transactions: general offers and schemes of arrangements (2014) *SA Merc LJ* 581.
[87]See EJ Weiss "Balancing interests in cash-out mergers: The promise of Weinberger V UOP Inc." (1983) *Delaware Journal of Corporation Law* 18.
[88]UK City Code rule 9.3.

procedures followed in SA and Delaware, a comparative analysis is difficult. Some of the problems relating to application of appraisal rights in South Africa have nevertheless been discussed in chapter 5.

6 5 Evaluating the arguments against the application of the mandatory offer in South Africa

The mandatory offer is opposed by a number of researchers but has its supporters. The debates on the rationales for the application of mandatory offer rules have been discussed in various chapters above and its connection with the equal opportunity rule was established in chapter 2 relating to US takeover laws. However, it is concluded that these rules do more harm than good in SA and Australia while the US is better off for not adopting a mandatory offer rule.

In respect of South Africa, Katz[89] questions the reason for implementing the mandatory offer rule. He questions the intellectual justification for implementing the rule. He further points out that the approach in the *Perlman* case was probably only justified by the special and unique facts of the case. Wiblin[90] comments that this may be one of those unfortunate cases where legislation is made based on a single case within a specific context. It is not clear if research was done to establish whether it was appropriate to apply the mandatory offer rule in South Africa. It appears that the rule was accepted as appropriate for implementation in South African markets without considering the differences between UK and South Africa's financial markets, such as the shareholding structures.

The assertions advanced by Dignam[91] relating to the distortion of the market for corporate control by concentrated share ownership structures, seem to be correct if one considers the proposed takeover of Adcock by CFR by means of

[89]MM Katz "Developments in corporate law" *Journal for Juridical Science (*1997) 22:2 *Journal for Juridical Science* 37.
[90]JR Wiblin "Mandatory takeover offer-too high a price for the economy to pay?" (2004) 29:3 *Journal for Juridical Science* 117*.*
[91]A Dignam "Transplanting UK Takeover Culture: The EU Takeover Directive and the Australian experience" (2007) 4 *International Journal of Disclosure and Governance* 148.

a scheme of arrangement in terms of section 114 of the Companies Act of 2008. The success of the scheme of arrangement was dependent on the support of major shareholders. At that time, a consortium led by the Bidvest Group Ltd was not in support of the scheme.[92] The attempted takeover of Adcock by CFR failed due to the fact that the consortium accumulated 34,5 percent of the shares, which then indicated that the scheme would not be successful as the consortium would not vote in favour of it, and approval of 75% of the votes of shareholders was required before the scheme of arrangement could pass.[93] However, it is suggested that had one of the major shareholders supported the scheme even prior to the consortium bid, the scheme of arrangement may well have succeeded. Large shareholders opposed to a takeover will make it difficult for a takeover bid to succeed. This results in a negative influence on the preference for the sale of corporate market control.

There appears to be a dearth of reliable information concerning control structures in companies.[94] This causes problems in assessing the extent of protection for minority shareholders and the equality of the corporate governance system prevailing within a country.[95] In SA, Luiz has pointed out that there is limited research about mandatory offers.[96] Researchers generally accept the assertion that large economies such as the US and the UK have dispersed ownership.[97] On the contrary, South Africa has concentrated share

[92]See SENS Further Cautionary Announcement regarding the cash offer by a consortium led by The Bidvest Group Ltd dated 3 December 2013 by Adcock. The announcement states that should the Consortium hold 25 percent of the voting shares of Adcock, the Consortium would have negative control. This on its own suggests that without the support of the Consortium – a potential major shareholder at that stage, the scheme would fail.

[93] See SENS announcement by Adcock and CFR dated 7 February 2014 relating to the joint announcement by Adcock and CFR on the termination of the proposal to implement the scheme of arrangement due to the fact that The Bidvest Consortium held 34,5 percent Available at: http://data.moneyweb.co.za/moneyweb/sharedata/scripts/sens.asp?id=227208 (Accessed on 20-3-2014).

[94]See M Massari, V Monge & L Zannetti "Control premium in the presence of rules imposing mandatory tender offers: can it be measured?" (2004) *Università Commerciale "Luigi Bocconi", MilanoIAFC – Institute of Accounting, Finance, and Control* 3

[95]Massari, et al (2004) *Università Commerciale "Luigi Bocconi", MilanoIAFC – Institute of Accounting, Finance, and Control*.3

[96]Luiz *An evaluation of the South African Securities Regulation Code on Takeovers and Mergers* LLD Thesis, Unisa. (2003) 727.

[97]See Armour & Skeel Jr (2007) *Georgetown Law Journal,* 1728-1729.

ownership structures.[98] Therefore, it can be argued that the impact of the mandatory offer rule on a UK company and a South African company will be different. The impact of the mandatory offer rule may discourage a change of control of a South African company. The large concentrated shareholding structures may require more mandatory offers to effect a change of control. This in turn requires large financial resources. Dispersed shareholding may have fewer mandatory offers. In light of the arguments put forward by researchers, questions may be asked as to the appropriateness of South Africa adopting the mandatory offer rule based on the UK rules. Concentrated ownership has been shown to consistently distort the market for ownership and control.[99] Therefore, the market for corporate control may not be as effective as it could be. The DTI 2004 Policy document, indicates that the new company law should be consistent with existing laws, including BBBEE legislation.[100] However, the retention of the mandatory offer section in its current form is not in line with the policy document. Any value enhancing BBBEE transaction is likely to be impeded by the mandatory offer requirement. This will be discussed in a separate paragraph below.

Even though the mandatory offer bid rule is intended to offer protection to minority shareholders when change of control occurs, there is no consensus on whether this can be achieved.[101] One of the reasons is that the mandatory offer reduces the number of value-increasing transactions for corporate control.[102] Offerors are unlikely to make a higher offer knowing that they face the possibility of having to make a mandatory offer at a higher price.[103] To avoid the high costs of a mandatory offer, such offerors will consider the implications of their

[98]See G Hertig & JA McCahery “Company and Takeover Law Reforms in Europe: Misguided Harmonization Efforts or Regulatory Competition?” (2003) *ECGI Working Paper Series in Law Working Paper* No. 12/2003. 4 and A Dignam “The globalisation of General Principle 7: transforming the market for corporate control in Australia and Europe” (2008) *Legal Studies* 96–118.
[99]Dignam (2008) *Legal Studies* 22.
[100]DTI 2004 Policy document.14.
[101]T Papadopoulos "The mandatory provisions of the EU Takeover Bid Directive and their deficiencies." (2007) *Law and Financial Markets Review* 528.
[102]528.
[103]528.

acquisition strategies before crossing the mandatory offer threshold.[104] They will try to acquire shares at a price below the premium as they know that they will be required to buy additional shares from the remaining shareholders at the same price. This action will deprive the minority shareholders of the very protection that the mandatory offer rule is supposed to provide.[105] Given the knowledge that there is an obligation to make a mandatory offer at the same offer price at which control was acquired from the controlling shareholders, an offeror is likely to reduce the premium to be paid to the controlling shareholder.[106] The reason why an offeror would pay a higher price is to be able to make a profit from the company. It is doubtful whether any rational businessperson will undertake an action, which will oblige him to pay more for less value.[107]

The strongest proponents of the deregulatory approach in takeovers are Easterbrook and Fischel,[108] who hold that any requirement for sharing of the premium reduces the likelihood that there will be any gains to share. In the US, the approach is that a majority shareholder is free to sell the controlling stake.[109] While it is acknowledged that minority shareholders may be negatively affected during the transfer of corporate control, it is also asserted that there are adequate corporate rules to prevent possible abuse.[110] In contradistinction to those countries enforcing the mandatory offer rule, the state of Delaware allows the market for corporate control to operate through the market rule approach.[111] Based on this approach, the new acquirer of corporate control determines the price it wishes to pay to the existing controller, without the sharing of a premium for control with other shareholders, required in the case of a mandatory offer bid. Corporate laws in the State of Delaware, adopt a director-centered

[104]528.
[105]528.
[106]Massari et al (2004) Università Commerciale "Luigi Bocconi", *Milano IAFC – Institute of Accounting, Finance, and Control* 4.
[107]Papadopoulos (2007) *Law and Financial Markets Review* 528.
[108]FH Easterbrook & DR Fischel "Corporate Control Transactions" (1982) 91 *The Yale Law Journal* 698.
[109]See *Zetlin v Hanson Holdings Inc*. Zetlin 48 N.Y.2d 684 (1979) Court of Appeals of the State of New York**.** See also the discussions under paragraph 2 2 above.
[110]Duke 1961 *Duke Law Journal* 560.
[111]See Schuster 2010 *LSE Law* 9*.*

approach towards takeovers and mergers. This gives directors discretion to decide on a merger or a takeover.[112] Corporate law also supports a dual approach to deal with approval of takeovers and mergers to deal with agency problems and the possible conflict of interests, particularly where directors are in the final stage of their tenure, as in transactions involving a change of control.[113] In those instances directors approve a merger followed by shareholder voting to protect the interests of shareholders interests. In a way, this is similar to the requirements for shareholder approval in cases of fundamental transactions.[114]

Mandatory offers have been labelled “bad for the market of corporate control, the freedom of establishment, and the integration of European equity markets in general.”[115] The mandatory offer rule has the effect of interfering with penetration of equity markets in Europe.[116] When corporate ownership is highly concentrated, the mandatory offer rule will tend to prevent corporate acquisitions: it becomes “in practice, an anti-takeover defense”.[117] Albuquerque and Schroth found, among other things, that the mandatory bid rule enforced in the EU, is not necessarily beneficial to shareholders.[118] The mandatory offer bid rule during a change of control is regarded as a protection from unfair expropriation for shareholders whose companies have dispersed share ownership may protect management from an effective challenge in companies with concentrated shareholder ownership.[119] Some scholars also reject the “highest price rules” advocated by the EU Directive as based on the UK City Code.[120] The ability of the mandatory offer rule to act as dampener for changes

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[112]Black & Kraakman 2002 *North Western University School of Law* 558.
[113]559.
[114]See discussions under paragraph Chapter 5
[115]Papadopoulos (2007) *Law and Financial Markets Review* 528.
[116]528.
[117]SM Sepe “Private Sale of Corporate Control: Why the European Mandatory Offer Bid Rule is Inefficient” (2010) *Arizona Legal Studies Discussion Paper* 10-29. 26.
[118]RA Albuquerque & EJ Schroth “Determinants of the Block Premium and of Private Benefits of Control” (2008) ECGI- Finance Working Paper No 202/2008; *Swiss Finance Institute Research Paper No.* 08-21. 2.
[119]See S Deakin “Corporate governance, finance and growth: Unraveling the relationship” (2010) *Acta Juridica* 217.
[120]Hertig & McCahery (2003) *ECGI Working Paper Series in Law Working Paper No*. 12/2003. 27.

of control that are disciplinary measures for ineffective directors has been discussed in detail in chapter 5 above.

6 6 Evaluating the dispute resolution procedures of the selected countries: The SA Takeover Special Committee, the UK Hearings Committee and the UK Takeover Appeal Board, and the Australian Review Panel

The UK Panel regulates all aspects of a takeover or a merger, including the discussions prior to the announcement of the transaction.[121] The day-to-day functions of the Panel are undertaken by the executives of the Panel who operate independently of the Panel.[122] The executives provide guidance on the interpretation, application and effect of the City Code.[123] Their procedures include resolution of disputes where the executives of the Panel issue rulings. The executives may also publish Practice Statements and provide non-binding opinions.[124] If parties do not agree with any decision, they may appeal to the Hearings Committee, and finally, to the Takeover Appeal Board (UK Appeal Board).[125] Proceedings before the UK Hearings Committee are usually private. The hearings are conducted in terms of the Rules of Procedure, which set various steps and how parties must conduct themselves during hearings. Although not usual, parties may be represented by legal advisers. Witnesses may be called with the consent of the chairman. The hearings are informal and there are no rules of evidence.[126] Rulings of the Hearings Committee are binding on the parties to the proceedings, unless and until overturned by the Takeover Appeal Board. Rulings may be published in the form of a Panel Statement.[127] Appeals against decisions of the Hearings Committee goes to the Appeal Board the UK Appeal Board is an independent body made up of three members.[128] The UK Appeal Board is created in terms of the UK City

[121]The UK City Code, Introduction.
[122]See UK City Code in 5 of the Introduction.
[123]See UK City Code in 6 of the Introduction.
[124]See UK City Code in 6 of the Introduction. It is indicated that the executives may among others, provide opinions and guidance on the interpretation of the City Code.
[125]UK City Code in 7 and 8 of the Introduction.
[126]See UK City Code in 7(b) of the Introduction.
[127]UK City Code in 7 of the Introduction.
[128]UK City Code in 8 of the Introduction.

Code. The procedures of the UK Appeal Board are set-out in its rules.[129] The hearing process of the UK Appeal Board is similar to that conducted by the Hearings Committee. Its rulings are issued as public statements. [130]

The South African Panel also regulates all aspects of an affected transaction or offer, including the resolution of disputes. The Executive Director of the Panel may perform any function of the Panel subject to the Act, the Takeover Regulations, policies and directions of the Panel.[131] The daily functions of the Panel are undertaken by the Executive Director and officers of the Panel.[132] The Executive Director or Deputy Director's decision may be appealed or reviewed by the TSC.[133] There is only one level of appeal as compared to that of the UK that has two levels for appeals.

The SA TSC is a committee of the Panel and is created in terms of section 202 of the Companies Act of 2008. Members of the TSC are not separate from those of the Panel. However, membership of the TSC is restricted to those members appointed by the Minister in terms of section 197(d). In addition, the chairperson is required to have certain qualifications.[134]

The primary focus of the Australian Takeover Panel is to resolve disputes during a takeover or a merger. The review and approval of takeover documents is undertaken by ASIC.[135] The Panel may review the decisions of ASIC.[136] The appeal, like those in the UK and South Africa, take the form of a rehearing. However, the review panel may not refer the matter back to the original panel.[137] Furthermore, the Australian Panel prefers written submissions rather than oral arguments.[138] The Australian Panel also prefers to accept

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[129]See also Takeover Appeal Board at www.thetakeoverappealboard.org.uk. (Accessed 20-12-2016).

[130]UK City Code in 8 of the Introduction.

[131]See section 200(2) of the Companies Act of 2008.

[132]See regulation 116.

[133]Section 202(3) of the Companies Act of 2008.

[134]See discussions in paragraph 5 3 of Chapter 5.

[135]See paragraph 4 2 3 of chapter 4 above, discussing bodies responsible for regulating takeovers in Australia.

[136]See paragraph 4 2 3 2 of chapter 4 dealing with Australian Panel.

[137]Calleja *The New Takeovers Panel – A Better Way?* (2002) 18.

[138]E Armson "Models for Takeover Dispute Resolution: Australia and the UK" (2005) 5 Part 2 *JCLS* 418-422.

undertakings to comply rather than make orders.[139] In contrast, in South Africa, it is common for parties to make written submissions followed by oral arguments.[140] In addition, the South African TSC issues written rulings and reasons for such rulings are the norm.[141] The TSC is not an appeal tribunal in the traditional sense. At a hearing of the TSC, the matter may be argued *de novo* and parties are not restricted to arguing the matter based on the papers submitted earlier. The TSC rehears the matter and new evidence may be submitted to it. The regulations are specific in that the South African Panel is not restricted to the laws of evidence.[142]

The process of regulating takeovers and mergers in Australia is formalistic compared to the UK, which has informal procedures.[143] Australian Panel proceedings are conducted like those of a court in an adversarial setting.[144] The panel deals with disputes between the parties in an adversarial setting. However, it is also pointed out that the panel proceedings are markedly different from a court process. The panel takes into consideration the need to deal with matters speedily, efficiently and fairly.[145]

Some researchers criticise the Australian Panel's proceedings as lacking transparency and not being up to the standard of what could be expected before a court.[146] However, such restrictions are based on efficiency concerns as they seek to encourage parties to provide complete information as quickly as possible. The restrictions are also aimed at avoiding an adverse effect on the market due to partial publicity. Often parties who attend the proceedings will have additional information about both companies, which is not in the public domain. This can result in unfairness for those parties who are not able to

[139]418-422.
[140]See Regulation 119(1).
[141]See Regulation 119(3) (c) which requires that the chairperson of the TSC must provide a written decision supported by reasons and a summary to the parties within a reasonable period.
[142]See Companies Regulation 119.
[143]Armson (2005) *JCLS* 421.
[144]E Armson "The Australian Takeover Panel: Commercial Body or Quasi-Court" (2004) *Melbourne University Law Review* 568.
[145]568-569.
[146]571.

attend the hearing.[147] During the hearing of the South African TSC, parties exchange a number of documents such as applicant submissions and claim document, respondent submissions, matters agreed, and heads of argument as if they exchange pleadings in a court case.[148] The TSC's proceedings are open to the public, unless one of the parties can justify that the proceedings should be held in private.[149] In addition, the regulations governing the proceedings are simple and do not resemble rules set for court proceedings, as they are controlled by the chairperson of the TSC. They may be conducted informally.[150] Often parties agree on a timetable for exchanging heads of argument.

However, some of the procedural steps such as the exchange of documents appear to be somewhat formalistic, even though the regulation provides for informal procedures.[151] It is asserted that the formalistic nature of South African proceedings can be attributed to the fact that the majority of the members of the TSC are practising attorneys and that the Companies Act of 2008 requires that an attorney or an advocate, whether practicing or not must be the chairperson of the TSC.[152] In some cases, junior and senior advocates represent parties that appear at TSC hearings. In a hostile takeover of Freeworld Coating Limited (Freeworld) by Kansai Paint Co. (Kansai), Freeworld and Kansai were each represented by a junior and senior advocate, and an additional team of attorneys.[153] The formalistic process of the South African panel is similar to that of the Australian Panel, where it has been indicated that the presence of a large number of lawyers on the panel influences procedures

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[147]569-570.
[148]See Regulation 119 and also the Ruling of the TSC in Country Bird Holdings Proprietary Ltd v Sovereign Food Investments Limited. Available on www.trpanel.co.za./rulings. (Accessed 8 - 8- 2017).
[149]In terms of regulation 119, the proceedings of the TSC are under control of the chairperson and may in appropriate circumstances rule on such a request.
[150]See Regulation 119 of the Takeover Regulations which provides for among other things: calling of witnesses; the informal nature of the hearing; who must preside and control the hearing; the *audi alteram partem;* recording and transcription of the hearing; decisions and written reasons for the decision and publication of the decision of the TSC, or the Panel.
[151]Takeover Regulation 119.
[152]Section 202(2)(a) of the Companies Act of 2008.
[153]See Ruling of the TSC in Country Bird Holdings Proprietary Ltd v Sovereign Food Investments Limited.

adopted by the panel. It frequently causes proceedings to become more complicated and procedural.[154]

Australian Panel proceedings are not legalistic and are aimed at promoting commercial interests. While the proceedings are formalistic, the Australian Panel also tries to discourage litigation attorneys from appearing at its proceedings and have issued a guideline in this regard. It is recommended that only commercial attorneys who advised the parties should be involved in panel hearings. Parties must obtain leave to be represented and this is normally granted.[155] The SA Takeover Provisions have no such restrictions during panel proceedings.

The participation of lawyers in Panel proceedings has raised some concerns in Australia. This is due to the fact that panel proceedings may be subject to tactical litigation.[156] Tactical litigation could result in delaying takeovers and mergers. This would be against policy considerations that takeovers and mergers should be regulated as efficiently as possible.[157] However, the counter argument is that lawyers may promote efficiency by facilitating that the Panel consider relevant legal and takeover policy issues.[158] The Australian regulations provides for procedures to deal with parties who misbehave during panel proceedings or who abuse panel proceedings.[159]

A comparison of the UK Panel hearing procedures indicates that they are better structured and more user friendly than those of South Africa. However, the Australian hearing procedures would be preferable for South Africa. The Australian regulations dealing with procedures for hearings are clear and detailed.[160] The Australian regulations place an emphasis on “speedy and

[154]Armson (2005) *JCLS* 425.
[155]423.
[156]423.
[157]See section 196 (2)(d) of the Companies Act of 2008.
[158] Armson (2004) *Melbourne University Law Review* 573.
[159]Australian Takeovers Panel, Panel Proceedings, (Australian Takeover Panel Procedural Rules) Available at: http//www.takeovers.gov.au. content/rules_for_proceedings/ default.aspx, (Accessed on 15-2-2014).
[160]See Australian Takeover Panel Procedural Rules.

quick" resolution of disputes. This requirement is considered to be one of the important cornerstones in the regulatory process and resolution of disputes. Proceedings must not be delayed unnecessarily.[161]

In addition, the Australian regulations appear to deal effectively with vexatious proceedings, whereas the South African regulations do not have equivalent or similar regulations. The role of the Australian Panel in resolving takeover disputes is a difficult one. This can be attributed to among others things: the adversarial nature of the dispute-resolution process, short time periods involved and the technical nature of takeover law, which is combined with consideration of policy issues. Procedural fairness is also important as it allows matters to be properly ventilated. Parties should have enough time to be heard.[162]

Even though the UK Panel is now a statutory body, its takeover dispute-resolution process still operates as it was when it was self-regulatory.[163] It operates differently from that of Australia.[164] The differences mainly relate to the extensive powers the UK Panel has. In addition, the UK Panel has powers to make and enforce its own takeover or merger rules. Even though there are differences between the two jurisdictions, the Australian and UK panels apply similar principles designed to ensure equal treatment of offeree shareholders, an informed market and proper conduct by offeree company directors. Both the regulatory systems rely mainly on non-judicial bodies to deal with takeover matters efficiently. The UK Panel procedures allow for a flexible process for dispute resolutions. Decisions are taken quickly and, according to Armour and Skeel Jr, in "real time."[165]

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[161]See Armson (2004) *Melbourne University Law Review* 569.
[162]569-573.
[163]L Gullifer & J Payne *Corporate Finance Law Principles and Policy* (2011)572.
[164]See Armson (2005) *Journal of Corporate Law Studies* 408-409.
[165]Armour & Skeel Jr (2006) *Centre for Business Research, University of Cambridge Working Paper* No. 331 2.

6 7 A brief evaluation of the enforcement measures for takeovers and mergers in the selected countries

The UK City Code makes it clear to parties involved in takeovers and mergers what their obligations entail. The UK City Code uses ordinary day-to-day English language. The use of legalese has been avoided.[166] The drafters considered that it is important for rules to be accessible to all since failure to comply with the provisions of the City Code is a serious transgression.

In the UK, a number of measures have been adopted to ensure compliance with the UK City Code. In some instances, where it is found that the circular sent to shareholders is deficient or does not comply with the City Code, parties may be required to correct the relevant documents and reissue the document to shareholders.[167] In addition, parties may be publicly censured, face disciplinary action, or be "cold shouldered".[168] These provisions are aimed at enforcing and discouraging non-compliance with the UK City Code. It is important that non-compliance be dealt with as speedily as possible.

The SA Panel does not have power to discipline, censure or "cold shoulder" any party. Instead, the SA Panel may, among other things: prohibit or require any action by a person, and order a person to divest of an acquired asset or account for profits;[169] issue compliance notices for infringements; refer the matter to the National Prosecuting Authority or other authority where it believes that an offence has been committed; issue a notice of non-referral to the complainant; or initiate legal proceedings.[170] It is an offence to fail to comply with a compliance notice issued by the Panel.[171]

The SA Panel may also bring a court action for the court to impose an administrative fine in terms of section 175 of the Companies Act of 2008.

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[166]See the UK City Code, and the rules thereunder. The UK City Code also has extensive explanatory notes for most of the rules.
[167]The UK City Code in 10 and 11 of the Introduction.
[168]The UK City Code in 10 and 11 of the Introduction.
[169]Section 119 (5) of the Companies Act of 2008,
[170]Section 170 of the Companies Act of 2008.
[171]Section 214 of the Companies Act of 2008.

Neither the UK Companies Act 2006 nor the UK City Code provides the UK Panel with such powers. In Australia, the power of enforcing takeover or merger provisions rests with both ASIC and the Australian Panel.

In SA however, the JSE Limited plays a limited role in approving circulars in respect of listed companies. For example, companies listed on the JSE Limited cannot remove their shares from the listing unless a general offer is made to shareholders and they be given an opportunity to exit the company at a fair price. However, where the approval of documents relates to other affected transactions, the Listings Requirements provides that the Panel must approve documents relating to takeovers and copies of documents sent to the Panel for approval and letters of approval from the Panel must be submitted to the JSE Limited.[172] However, as indicated in 5 8 above, the enforcement powers of the SA Panel could be enhanced and made more efficient if the rulings of the TSC could be enforced in a similar manner as those of the Financial Services Tribunal established under section 219 of the Financial Sector Regulation Act 9 of 2017. In Australia, ASIC as a main administrator of the Corporations Act 2001, has extensive powers in terms of that legislation. According to the information sheet from ASIC:

> "The ASIC Act directs ASIC to 'take whatever action it can take, and is necessary, in order to, enforce and give effect to the laws of the Commonwealth that confer functions and powers on it'."[173]

The Australian Panel has powers to declare unacceptable circumstances in relation to a takeover or merger. Following the declaration, the Panel may then order additional disclosures, cancellation of contracts or even freezing of transfers of assets resulting from the transaction.[174] Section 119(5) of the

[172]See JSE Limited Listings Requirements sections 9.30-931.
[173]See Australian Securities Exchange and Investment Commission, Available at: http://www.asic.gov.au/asic/pdflib.*nsf*/LookupByFileName/INFO_151_ASIC_approach_to_enforcement_20130916.pdf/$file/INFO_151_ASIC_approach_to_enforcement_20130916.pdf> (Accessed on 10-10-2014).
[174]See discussions in chapter 4 dealing with powers of the Australian Panel in terms of section 602 of the Corporations Act 2001.

Companies Act of 2008, gives the Panel teeth to ensure compliance. In terms of the section, the SA Panel may prohibit and require any action by a person or order a person to divest of an acquired asset, or account for profits.

The Australian takeover provisions create absolute liability offences for contravention of certain provisions.[175] The courts enforce the Australian Panel's orders and panel rules.[176] The UK Panel has powers to issue compliance rulings and compensation rulings in certain circumstances.[177] The UK Panel also has disciplinary powers in terms the UK City Code.[178] The UK Panel may also approach the courts to enforce its rules.[179]

6 8 A brief evaluation of the role of the courts in the regulation of takeovers and mergers in the selected countries

In the UK and Australia, takeovers and mergers are the domain of specialist commercial regulators, rather than the courts. In contradistinction to the US, the role that the courts play during a takeover or a merger in jurisdictions is limited. In evaluating the role of the courts in the US during a takeover or merger, one should not lose sight of the fact that the various standards of reviewing the decisions of the boards of directors were developed by the Delaware courts in order to protect shareholders from certain actions of directors. Such an approach is not suitable for SA.[180] Accordingly, while it may be appropriate for SA to adopt certain US provisions such as appraisal rights, it would not be appropriate to have the courts as primary regulators of takeovers and mergers. However, the standards of reviewing directors' conduct during takeovers and mergers created by Delaware courts, would be useful in preventing conflicts and promoting transparency during a takeover or merger

[175]See E Armson "Before the High Court: Attorney-General (Commonwealth) v Alinta Limited: Will the Takeovers Panel Survive Constitutional Challenge?" (2007) 29 *Sydney Law Review.* 499.
[176]See Armson (2007) *Sydney Law Review.* 499.
[177]UK City Code in 10(b) and (c) of the Introduction.
[178]UK City Code in 11 of the Introduction.
[179]Section 955 of the UK Companies Act 2006 and UK City Code in 10(d) of the Introduction.
[180]See Boardman (2010) *Acta Juridica* 325.

in the SA context. This would further enhance protection of minority shareholders. In particular, the requirement that the board must be well informed about a takeover or a merger before requesting shareholders to vote on it[181] and the requirement that an independent, well informed, fully empowered special committee must consider certain takeovers and mergers could be of considerable value to shareholders in South Africa.[182] Unlike in countries where a mandatory offer rule is enforced and where separate regulatory bodies actively enforce takeover and merger rules, the courts in Delaware are central to enforcing the various corporate law rules, including those applicable during takeovers and mergers.[183] Accordingly, the courts have inter alia developed the important principles that deal with conflicts of interests of directors during takeovers and mergers.[184]

In the UK, the courts may not interfere with the takeover or merger process, in accordance with the principles established in the *Datafin case*.[185] There is a restraint on the courts' power to review the decisions of the UK Panel during a takeover. The UK Panel, which enforces the UK City Code – has exclusive jurisdiction on regulation of a takeover while such a takeover is in progress. The implementation of the EU directive has no effect on this rule.

The Australian Panel has exclusive jurisdiction during the course of a takeover or a merger.[186] The panel may, however, refer questions of law to the courts. The Australian Corporations Act 2001, in section 659AA, restricts the role of the courts during a takeover or a merger. Section 659AA of the Corporations Act 2001 provides that only certain specified governmental agencies may bring a matter before the courts. In addition, section 659C of the Corporations Act

[181]See Smith v van Gorkom, 488 A.2d 858 (Del 1985, a decision of the Delaware Supreme Court.
[182]See *Kahn v M & F Worldwide Corp,* 88 A3d 635 (Del 2014), a decision of the Delaware Supreme Court
[183]See the discussions under paragraph 2 3 1.
[184]See discussions dealing with the standards of reviewing directors conduct during takeovers and mergers created by Delaware courts under paragraph 2 5.
[185]*R v The Panel on Takeovers and Mergers, ex parte Datafin plc and another* 1987 QB 815. See also Gullifer & Payne *Corporate Finance Law Principles and Policy* 568.
[186]Armson (2005) *JCLS* 408.

2001 limits the powers of the courts to make certain orders following the completion of a takeover bid. The courts may not unwind a merger or a takeover. Where there is a finding that the Corporations Act 2001 has been infringed during a takeover or merger, the court can only order a remedy in the form of monetary compensation as indicated in chapter 4.[187]

The SA Companies Act of 2008, unlike the Australian Corporations Act 2001, is silent on whether or not courts may intervene in a takeover or merger process. The legislature left it to the courts to decide whether or not to allow offerors to approach the courts during the course of the takeover or merger process. A brief review of previous court cases indicates that in appropriate circumstances offerors may approach the courts and stop an offer prior to its completion. In the *Gold Fields* case,[188] court intervention resulted in a hostile takeover bid being defeated. Briefly, in the attempted hostile takeover of Gold Fields Limited (Goldfields) by Harmony Gold Mining Company Limited (Harmony), Gold Fields adopted various legal tactics to prevent a hostile takeover. The tactics included approaching various regulatory authorities, such as, the Competition Authorities and the then SRP, the predecessor to the Takeover Regulation Panel, and finally the courts.[189] The matter culminated in Gold Fields succeeding to defend the hostile takeover. Gold Fields won the case when the court held that the period within which the takeover bid had to be made had expired, and such a period could not be extended.[190] The legal tactics eventually led to the hostile bid being prevented. The takeover bid did not fail because shareholders did not like the price offered. The shareholders did not have the opportunity to choose between accepting or rejecting the offer from Harmony. The attempted takeover failed due to the fact that the directors of the offeree company prevented the shareholders from making their own choices about the merits of the offer.

[187]Armson (2009) *Melbourne University Law Review* 661.
[188]*Gold Fields Ltd v Connellan NO* [2005] 3 All SA 142.
[189]A L Christison & RC Williams "The Harmony –Gold Fields Take -over battle" (2008) *SALJ* 790- 822.
[190]*Gold Fields Ltd v Connellan NO* [2005] 3 All SA 142.

Another attempted hostile takeover involved Protech Khuthele Holdings Ltd, the target, and Eqstra Holdings Ltd – the offeror. The offeree company approached the courts to challenge the takeover on the basis of a contract entered with its BBBEE partners. The hostile bid was subject to a condition precedent that shareholders holding more than 50 percent of the issued shares accept the offer before the offer could be implemented. The offeree company argued that in terms of the contract with the BBBEE party, (which was also one of the significant shareholders), the BBBEE party could not accept the offer in terms of the agreement with the company.[191] The court proceedings caused delays, and this in turn resulted in the hostile bid failing as the time period for the bid had expired. The hostile offeror had to terminate the offer.[192] It is suggested that the failure to meet the conditions relating to the percentage of shareholders who accepted the offer, was influenced by the uncertainty created by the court proceedings. Until the court proceedings had been resolved, shareholders would have been reluctant to tender into the offer and accept the offer since they would not have been certain when they would receive payment. Shareholders would prefer to hold on to their share portfolios until the uncertainties have been resolved.

In yet another attempted takeover of Adcock Ingram Limited (Adcock) by CFR Pharmaceuticals SA (CFR), it was reported that the Bidvest Group Consortium was threatening to challenge the proposed scheme of arrangement to be entered into by Adcock and CFR before it was implemented.[193] According to reports in the financial press, court papers were served on some of the parties with the aim of preventing the implementation of the scheme transaction. In

[191]BBBEE agreements are subject to funding arrangements involving a number of parties including the beneficiary company. Such agreements often restrict the ability of BBBEE partners to vote or sell their shares unless parties agree otherwise.

[192]See Announcement to shareholders of Protech Khuthele Holdings Ltd from Eqstra Holdings Ltd about the details of the hostile offer dated 21 February 2013 Available at http://data.moneyweb.co.za/moneyweb/sharedata/scripts/sens.asp?id=208573>, and a response announcement from Protech Khuthele Holdings Ltd to its shareholders dated 5 December 2013, and finally a SENS announcement dated 1 August 2013 from Eqstra HoldingsLtd,Availableat:http://data.moneyweb.co.za/moneyweb/sharedata/scripts/sens.asp?id=21737 (Accessed 20-3-2014).

[193]BizNews.com. “Bidvest’s legal challenge –executive summary of papers served to spike CFR’s guns on Adcock takeover” November 2013 Available at (http://www.biznews.com/archives/2013/11/ Accessed 20-3-2014).

addition, the application requested, among others, orders that the scheme be declared void and that the scheme meetings were not properly convened.[194] The announcement of a court application on its own raised uncertainty for parties involved and the affected shareholders as to how such an application would impact the scheme of arrangement once the scheme was approved by the shareholders.

These cases illustrate that it is possible for unwilling offeree companies to adopt tactical litigation to defeat takeovers. Takeover law should not facilitate such tactical litigation, as these are prejudicial to offeree-company shareholders.
It is suggested that court orders to unwind mergers create unnecessary uncertainty in the market for corporate control. In Australia, the courts' powers are limited to awarding damages rather than to unwind a transaction.[195]

6 9 Mandatory offer and Broad Based Black Economic Empowerment

Of particular importance, and relevance, to South Africa is that the effect of the mandatory offer requirement on Broad Based Black Economic Empowerment (BBBEE)should not be underestimated. Acquisitions of shareholdings by BBBEE beneficiaries in this context do not refer to the mere handing over of shares by one party to another person. Financing of significant BBBEE transactions remains one of the stumbling blocks to economic transformation in South Africa.[196] Therefore, where a mandatory offer is required, funding to pay for additional shares for such deals may not be available. It is generally acknowledged that raising funding to acquire shares to implement a BBBEE transaction is expensive and difficult, and that parties and funders to such transactions often resort to some innovative funding structures.[197] The

[194]SENS Announcement by Adcock dated 4 December 2013
Available at: http://data.moneyweb.co.za/moneyweb/sharedata/scripts/sens.asp?id=224531> (Accessed 20-3-2014).
[195]Armson (2009) *Melbourne University Law Review* 661.
[196]See NE Phillips *The funding of Black Economic Empowerment in South Africa.* Unpublished Thesis presented in fulfillment of the requirements for a Masters' Degree in Economics at the University of Stellenbosch (2004). 42.
[197]See Phillips *The funding of Black Economic Empowerment in South Africa*. In this research, it is indicated that BBBEE funding methods are not sustainable and often results in participants of such transactions not benefiting. Chapter 2, pp 33-52.

requirement for a mandatory offer makes an acquisition of a meaningful stake expensive.[198] The mandatory offer rule raises the costs of implementing BBBEE share ownership transactions.[199]

For South Africa, it has been suggested that there is no good grounding for the mandatory offer rule.[200] The Van Wyk de Vries Commission, whose work culminated in the introduction of the rule into South African legislation, emphasised the protection of minority shareholders.[201] It is suggested that the possibility that the rule may impede the wider share ownership by previously-disadvantaged groups was not considered. This fact should not be surprising due to the political and economic imperatives at that time. The SAC later raised this concern but it was ultimately decided that the rule should be retained.[202] Still, it is submitted that as the imperative of BBBEE gains even further momentum, it should be asked whether it is not time to reconsider the rule as it undermines BBBEE.

One of the differences between the mandatory offer requirements of the UK and South Africa is the trigger threshold.[203] It is asserted that this ensures that BBBEE parties are not required to make a mandatory offer due to the fact that many BBBEE transaction are aimed at holdings of one- third of the voting rights.[204] It is doubtful that this could have been intended to accommodate BBBEE transactions because the mandatory offer rule was in existence even before the BBBEE policies were introduced. The threshold of 35 percent is not new, as it was set in the SRP Code and the Companies Act of 1973.[205] It also does not appear from the DTI 2004 Policy document that BBBEE share ownership and the impact of the mandatory offer rule on such initiatives were

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[198]M Lepaku "Mandatory offers and BEE" (2005) 13 (4) *JBL* 170-171.171.
[199]See Wiblin (2004) *Journal for Juridical Science* 183.
[200]Katz (1997) *Journal for Juridical Science* 28-41.
[201]Luiz (1997) *S A Mercantile Law Journal* 239-264.
[202]Minutes of the SRP held on 4 March 1997. At this meeting, the members of the SRP discussed the issue at length at agreed that the mandatory offer rules should be retained. Members also agreed to prepare a paper setting out the reason for retaining the rule.
[203]Boardman (2010) *Acta Juridica* 324.
[204]324.
[205]See discussions on this point under chapter 5 on 'affected transaction' in terms of section 440A (1) of the Companies Act of 1973 and the SRP Code.

considered.[206] If the suggestion is that the BBBEE parties should be satisfied with less than 35 percent in order to avoid the mandatory offer rule, then the provision is clearly inadequate when it comes to the promotion of BBBEE. Although the 35% threshold to some extent ameliorates the impact of mandatory offers on BBBEE transactions, the share ownership of BBBEE shareholders should not be artificially limited to 35 percent. BBBEE is not about merely obtaining the minimum shareholding required by various BBBEE Codes but acquisition of meaningful shareholding by black groups. The mandatory offer rule is hampering such acquisitions.

Further, as discussed in paragraph 5 6 9 4 of Chapter 5, according to the ruling in the *MGX case*,[207] the interpretation of “parties acting in concert” is broad. Accordingly, a wide range of parties may become subject to the mandatory offer rule because of the wide definition of the phrase “acting in concert”. Within the South African context, this broad definition of the concept makes the mandatory offer rule broader and limits the ability of BBBEE parties to raise funding. A funder may be regarded as a “concert party” and may be liable to make a mandatory offer even though the intent was to merely facilitate the acquisition of a meaningful stake for the BBBEE shareholders, and not to acquire control. This may create a further obstacle for funding for BBBEE transactions.

The findings by researchers about the resistance to changes in patterns of share ownership in South Africa, despite the existence of the laws to promote BBBEE can be explained by reference to important theories that explain the reasons for such resistance. One of the theories relate to path dependency of laws. According to Hathaway[208]

> “In broad terms, “path dependence” means that an outcome or decision is shaped in specific or systematic ways by the historical path leading to it. It entails, in other words, a causal relationship between stages of temporal

[206]See DTI 2004 Policy document.
[207]*Securities Regulation Panel V MGX Limited* WLD Case NO 1602/03.
[208]OA Hathaway “Path dependence in the Law: The course and pattern of legal change in a common law system” (2001) 86 *Iowa Law Review* 603- 604.

> sequences, with each stage strongly influencing the next stage. At the most basic level, therefore, path dependence implies that "what happened at an earlier point in time will affect the possible outcomes of a sequence of events occurring at a later point in time"[209]

Path dependence can result in locking of decisions and resistance to changes. This inflexibility can lead to inefficiency when legal rules fail to respond to changing conditions.[210] This appears to be in line with the assertion of Bebchuk and Roe,[211] that existing rules may heavily influence new rules. They point out that:

> "A country's legal rules at any point in time, might be heavily influenced by the ownership patterns that the country had earlier; The efficient ownership structure for a company is often path dependent; The relative efficiency of alternative ownership structures depends partly on the structures with which the company and/or other companies in its environment started; Those parties who participate in corporate control under an existing structure might have the incentive and power to impede changes that would reduce their private benefits of control even if the change would be efficient. For example, a controlling shareholder might elect not to move her firm to a diffused ownership structure because the move would reduce the controller's private benefits of control."[212]

These findings have important implications for the implementation of initiatives to promote the economic participation of black people, such as BBBEE share ownership. Such initiatives have little chance of success, unless supported by existing shareholders. However, it is not necessarily in the interest of some of the shareholders to support such initiatives as they interfere with their private benefits. It is of course true that the mandatory offer rule may also offer protection for BBBEE shareholders that are shareholder offerees in takeovers. However, this argument does not justify maintaining the mandatory offer rule because a) of the urgent need to grow meaningful BBBEE shareholding in

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[209]603- 604.
[210]603- 604.
[211]L Bebchuk & M Roe "Theory of Path Dependence in Corporate Ownership and Governance" (1999) *Discussion Paper No. 26610/99, Harvard Law School*. 3.
[212]Bebchuk & Roe (1999) *Discussion Paper No. 26610/99, Harvard Law School.* 3.

companies and b) the relatively low level of shares held by BBBEE beneficiaries. Furthermore, it may be argued that other regulations such as appraisal rights may also serve as a disincentive for BBBEE and they are subject to similar criticisms. However, the appraisal right process does no more than to allow the shareholder to receive a fair value for his shares. The cost of having to react to appraisal rights may complicate BBBEE transactions but probably not to the same extent as mandatory offers. The main problem with mandatory offers is that they vastly increase the cost of control transactions. This distinction is particularly important if it is considered that major shareholders who are aware of the potential benefits that their BBBEE transaction will add to the company, will adopt a tactical strategy to defeat such a transaction through exercising their appraisal rights. At least the risk that an exercise of an appraisal right may be costly for the offeree in comparison to the gains achieved from it may keep the exercise of these rights within reasonable bounds. At least appraisal rights are only restricted to fundamental transactions.

The requirement to pay the same price in terms of the mandatory offer rule prevents transfer of control to BBBEE and therefore, partly contributes to the failure of initiatives to spread share ownership among listed companies. The previous situation whereby certain groups were not able to participate in the financial markets is maintained by the enforcement of the mandatory offer requirement. Therefore, this supports the argument that rules are path dependent, as postulated by some researchers.[213] The existence of the earlier established mandatory offer requirement influences the implementation of BBBEE share ownership in line with the path dependence theory.

Further, the initial legal and political structures affect future corporate rules, which in turn affect future decisions on corporate structures. As Bebchuk and Roe[214] point out, "the concern is with the corporate rules system "in action" rather than "on the books". Therefore, policy makers should be aware of the

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[213] 1.
[214] 24.

totality of the rules, which may be an impediment to their efforts in changing the economic environment. The role of interest groups in influencing existing and old laws has been argued as that their choices might sometimes lead to inefficient rules being chosen or maintained.[215] Political interactions of those interest groups depend on the existing pattern of corporate ownership.[216] Various interest groups will try to protect and maintain their interests by forcing the retention or change of certain laws, depending on whether those laws threaten or promote their interests.[217] In this regard, the relative power of each interest group is important in influencing the direction of laws. Due to the fact that interest groups differ in their ability to get support and exert pressure in favour of or against certain laws, the groups with more resources will tend to be more successful.[218] These dynamics are suggestive of some of the reasons why the existing distribution of wealth and power plays an influential role in the rules chosen. Corporate laws of a country may therefore depend on the economy's earlier existing corporate structures.[219] The above discussions suggest that South Africa should take into consideration some of these stumbling blocks when it enacts legislations intended to achieve economic changes. The detailed discussions on the dynamics, in respect of South Africa, on the role played by various interest groups are beyond the scope of the dissertation, however a few brief observations on this topic is justified.

The structure of corporate law in any given country is a consequence of that country's particular pattern of corporate ownership, which is, in turn, determined, at least in part, by forces outside corporate law.[220] Further, patterns of ownership structures shape corporate law in two ways. Firstly, interest groups will distribute larger portions of company fruits to themselves and secondly, "share ownership patterns shape the problems to which reforms designed to facilitate investment respond".[221] The fact that certain groupings

[215] 24.
[216] 25.
[217] 25.
[218] 28.
[219] 26.
[220] 33.
[221] 23- 24.

will have more wealth means they will have more influence over corporate laws that are chosen. Inevitably, these interest groups will more likely choose corporate laws which favour the retention of existing corporate structures where these structures are the ones that ensure protection of their interests.[222]

In certain instances, corporate rules affect ownership and governance structures in different ways.[223] These may include facilitating concentrated share ownership structures.[224] This is relevant where controlling shareholders benefit from private benefits. In such a case, controlling shareholders will be reluctant to lose control.[225] Therefore, such controlling shareholders are more likely to favour existing corporate rules, such as, the mandatory offer rule, which protect their position. By making control costly, it ensures that the existing controlling shareholders continue enjoying private benefits. Controlling shareholders are unlikely to support initiatives aimed at distributing share ownership to the broader community. Referring to the rules which encourage maintenance of concentrated share ownership, such as, the mandatory offer rule, some researchers point out that controlling shareholders are likely to have more resources and will use those resources to ensure maintenance of concentrated share ownership.[226]

Scholars point out that control over corporate decision-making and resources also provides political power.[227] Interest groups such as controlling shareholders or professional managers are likely to have more influence because of the resources that they have under their command. These resources enable them to lobby, contribute to political campaigns and even gain political influence. These resources could also provide those interest groups with visibility, access to media, ability to raise their social status, and access to elite and influential groups.[228] All these actions assist these interest groups to

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[222] 24.
[223] 24.
[224] 28.
[225] 28.
[226] 23-24
[227] 23-24.
[228] 28.

influence the corporate laws to what is suitable and beneficial to them.[229] Those in control of companies can push to retain or expand legal rules that favour them. This in turn ensures that existing patterns of ownership are retained.[230] Interest groups choose laws and structures that will benefit them.[231] This suggests that where there is a pattern of concentrated ownership, programmes aimed at encouraging dispersed ownerships may be impeded and, similarly, where there are dispersed ownership structures, such structures may be maintained. This will be dependent on what the interest group perceives as a threat to their interests.

Roe[232] suggests that it would be wrong to ignore the societal and political considerations, when trying to find reasons why one firm succeeds while another fail. Extrapolated to government policies, this means that where governments are trying to implement certain policies, it is imperative that policy makers not disregard societal and political contexts within which corrective initiatives are undertaken. It has also been pointed out that, in some instances, the legal system is isolated from social and economic change.[233] This suggests that policy makers in South Africa should be careful when effecting various proposals for economic reforms and improvement. The economic impact and efficacy of such programmes in assisting economic development should be considered, based on work of researchers from other disciplines, such as, economics and sociology.

[229] 27
[230] 23-24.
[231] MJ Roe "Political Preconditions to Separating Ownership from Corporate Control" (2000) 53 *Stanford Law Review* . 42 Columbia Law and Economics Working Paper No 155 Available at: SSRN: http//ssrn.com/abstract=16543 (Accessed 20-3-2014).
[232] MJ Roe "Political Determinants of Corporate Governance: Political Context, Corporate Impact" (2003) Harvard Law School John M. Olin Center for Law, *Economics and Business Discussion Paper Series*. Paper 451. 1-3. Available at: SSRN: https://ssrn.com/abstract=472366.235. (Accessed 20-3-2014.
[233] P Lipton "A History of Company Law in Colonial Australia: Economic Development and Legal Evolution" (2007) *Melbourne University Law Review* 830.

6 10 Concluding remarks

The evaluation in this chapter indicates that similar issues among comparative countries influenced the development of regulations for takeovers and mergers. The general aims include, to encourage confidence and integrity in financial markets by combating any type of fraud, market abuse and misinformation of investors. While it is generally accepted that takeovers and mergers must be regulated, countries are, however, no closer to finding an effective regulatory regime. This is not surprising as jurisdictions face numerous complexities in designing a suitable regulatory regime. In the case of the EU, arbitrage and regulatory competition also plays an important role in decisions to determine which regulatory regime to implement. This may result in companies choosing countries which allow innovative takeover rules. [234] Therefore, countries have to balance the interests of their corporate citizens against the harmonisation of rules relating to protection of shareholders in general.[235]

Naturally, most countries will lean towards policies that protect their own companies and shareholders. Hence, the view has been expressed that the EU Takeover Directive "is likely to be ineffective or to promote bureaucratic uniformity rather than enable market-driven diversity."[236] According to Ferrell,[237] the US and the UK's experiences of adopting takeover regimes is important. One of the lessons that can be learnt is that, in designing a takeover regime, substitutes must be considered having regard to any negative impact such rules may have on other specific legal rules aimed at achieving identified goals. For SA, the mandatory offer requirement should be considered in this vein.

The US and Australia have developed different takeover and merger regulatory systems from those of the UK. Presumably, these regulatory regimes have

[234] See Hertig & McCahery (2003) *ECGI Working Paper Series in Law Working Paper N*o. 12/2003.34.
[235] 24.
[236] 3- 4.
[237] A Ferrell "Why Continental Takeover Law Matters" (2003) *Discussion Paper No.454 12/2003, Harvard Law School, Cambridge, MA 02138:* Available at: http://www.law.harvard.edu/programs/olin_center/ (Accessed 20-3-2014).

been adopted because they serve those countries' economies and financial markets better. Even though there are differences between the SA takeover and merger provisions and their UK counterpart, the South African provisions have closer similarities to those of the UK than any other comparative country. This is not surprising considering that the early SRP Code was transplanted word-for-word from the City Code.[238] The introduction of the Companies Act 2008 and the takeover regulations has not significantly changed the earlier transplanted takeover rules.[239] Therefore, the influence of the UK City Code is still evident in the South African takeover and merger legislation in the Companies Act 2008 and the Takeover Regulations.[240] This is despite the marked differences in the ownership structures, economies and social and developmental needs of South Africa as opposed to the UK.

The UK City Code had been operative for some years before chapter 6 of the Australian Corporations Act 2001 was promulgated. It is also generally accepted that the method for regulating takeovers and mergers set-out in the City Code is widely applied by many countries. Some of its provisions have also been adopted by the EU and have been incorporated in the EU Takeover Directive.[241] However, despite these accolades, rather than adopting the UK model for regulation of takeovers and mergers, Australia chose a different path towards achieving an effective takeover and merger regulatory model. It is suggested that Australian policy makers took into account their own cultural and economic considerations and chose to tailor-make their own takeover provisions that would be suitable for their financial markets. Regulations for takeovers may differ depending on:

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[238]See Introduction to the repealed SRP Code indicating that the SRP Code is based on the UK City Code.
[239]See Deakin (2010) *Acta Juridica* 216.
[240]See discussions by Boardman (2010) *Acta Juridica* on the provisions of the Companies Act of 2008 and the UK Companies Act 2006 and the UK City Code.
[241]See P Bockli, P Davies, E Ferran, G Ferrarini, J Garrido Garcia, K Hopt, A Pietrancosta, K Pistor, R Skog, S Soltysinski, J Winter and E Wymeersch, European Law Experts "Response to the European Commission's Report on the Application of the Takeover Bids Directive" (2014) *University of Cambridge Faculty of Law Legal Studies*. Paper No.5/2014 3. Available http://www.law.cam.ac.uk/ssrn (Accessed 20-3- 2014).

> "[T]he varying historical and cultural contexts in which the regulation developed and differing emphasis and assessments of priorities."[242]

Political considerations also play an important role in determining the type of laws to be adopted.[243] This is important for South African policy makers as, ignoring historical context of legal development may negatively affect development of new laws. Closer political ties between countries may well result in the adoption of another country's laws, even though its economies and markets may be different to those of the country from where the laws originate. This appears to be applicable in the case of South Africa's adoption of the mandatory offer requirement. Historically, the UK has close political ties with SA and, therefore, it may have been convenient to adopt some of their rules, such as the mandatory offer requirement, without considering the impact of these laws on South Africa's economy and its financial markets. From the deliberations of the SAC, it appears that the existing relationship leads to the continued application of the mandatory offer.[244]

Corporate governance systems should not be adopted merely on the assumption that because they are effective for a particular country, they also will be beneficial for another country. The unique cultural, social and economic needs of each individual country must be accommodated within the corporate governance systems if such systems are to be accepted by the citizens of those countries. Olson[245] points out that:

> "[W]hat is 'wrong'win Delaware or England may be entirely appropriate for South Africa, just as what works well in South Africa may not work in the culture of Germany or Australia. There is and should be room for national variations in the thrust and content of corporate governance prescriptions. In South Africa, it seems clear to this observer, as a direct result of the relatively recent

[242]Armson (2005) *JCLS* 402.
[243]R La Porta, F Lopez-de-Silanes & A Schleifer (1998) *Journal of political economy* 1145.See also Bebchuk & Roe (1999) *Discussion Paper No. 26610/99, Harvard Law School.*
[244]See discussions in paragraph 5 6 9 3 where the SRP indicated that it must keep with international standards.
[245]Olson "South Africa moves to a global model of corporate governance but with important national variations" (2010) *Acta Juridica* 247.

> establishment of a just and diverse political system and related changes to the nation's social and economic structures, that concerns of the Companies Act for promotion of broader economic and social benefits than corporate profitability, and for worker and another stakeholder representation, are understandable and appropriate."[246]

In this regard, one needs to consider that the US and the UK have divergent corporate systems despite economic, legal and cultural similarities.[247] Therefore, it is important that South African policy makers realise that "social needs and regulatory responses will inevitably be bound up with each other".[248] The mandatory offer rule negatively affects the aims of reducing the socio-economic inequalities in the country, and creates an unhealthy tension with other legislation seeking to promote BBBEE. According to research, it is unlikely that a significant number of BBBEE transactions will be achieved unless some of the stumbling blocks are removed.[249] Abolishing or relaxing the application of the mandatory offer rule could be one such initiative. The role of takeovers in promoting efficient markets and good governance would also be promoted.

The existing patterns of share ownership influence the future of this ownership scheme and hence determine the success or failure of policies aimed at distributing share ownership. As can be seen from the arguments presented in this chapter, the mandatory offer rule assists in the preservation of undesired patterns of ownership in SA. Existing constraints may frustrate efforts to ensure justice and equity in the economy through, among other things, broad-based share ownership. Bebchuk and Roe[250] assert that:

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[246]Olson (2010) *Acta Juridica* 247.
[247]Bruner (2010) *Virginia Journal International Law* 583.
[248]590.
[249]See Lipton (2007) *Melbourne University Law Review* 830. See also Phillips *The funding of Black Economic Empowerment in South Africa,* who discusses the various obstacles relating to financing meaningful shareholding by BBEEE participants. Chapter 2 pp-33-52.
[250]Bebchuk & Roe (1999) *Discussion Paper No. 26610/99, Harvard Law School*. 3.

> "Path dependence is an important force—one that students of comparative corporate governance need to recognise—in shaping corporate governance and ownership around the world."

Hertig and McCahery[251] support the view that the differentiation of corporate governance systems is necessary, and that the needs of each individual country have to be taken into account in corporate reform initiatives. Writing on the implications of transplanted laws in the context of the EU, Hertig and McCahery deal with the EU Takeover Directive and point out the following:

> "[T]here is no simple model for corporate regulators to use when designing reforms. While current efforts to modernise European Union (EU) company law and to create a takeover regime are influenced by shareholder value maximisation considerations, one must not forget that there are political barriers to transplanting the Anglo-Saxon approach in continental Europe. Given the important differences between corporate governance systems in Europe, the appropriate regulatory approach is to provide firms with the freedom to select the regulatory environment that suits their needs."[252]

Of relevance to SA, Bruner holds that :

> "[T]he use of comparative analysis to generate claims about what a given country's regulatory system ought to do is fraught with complex problems and, in particular, that social, cultural, and political variables are often airbrushed out of the picture to facilitate straightforward cross-border comparisons. As the foregoing discussion suggests, comparative analyses ignoring the impact of political context will inevitably present a distorted picture, resulting in unsupported claims regarding what the future might bring."

He therefore, indicates that:

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[251]Hertig & McCahery (2003) *ECGI Working Paper Series in Law Working Paper N*o. 12/2003. 4.
[252]4.

> "[R]regulatory divergences may actually reflect variation in the social needs and problems that each society aims to address through the corporate governance system." [253]

This assertion tends to support a view that it is acceptable for countries to differ in respect of corporate governance measures. Therefore, it is necessary for SA to introduce corporate governance systems that are aimed at achieving particular societal goals, namely, that of contributing to the reduction of the high economic inequality in the country, and it should be acceptable that different corporate governance measures should be adopted. The continued application in SA of the mandatory offer rule based on the UK's City Code should be seriously questioned. Differences in the economies and financial markets and SA's unique social and economic developmental needs, justify a different approach in SA.

[253]Bruner (2010) *Virginia Journal International Law* 592.

Chapter 7: Conclusions and recommendations

"South Africa's path toward sustainable economic development requires a sound legal structure for governance of its businesses – a structure that complements and supports the continuing development of a diverse, equitable political system and respects South Africa's distinct social needs."[1]

7 1 Conclusions

This dissertation researched regulation of takeovers and mergers with an emphasis on the mandatory offer rule, specifically its impact on the market for corporate control in South Africa. This concluding chapter recaps the discussions and conclusions arrived at in the preceding chapters. It then makes recommendations in respect of the mandatory offer rule, the takeover and merger provisions in the Companies Act 2008 and the Takeover Regulations. From the literature review and the comparative research, a number of conclusions has been made in each chapter and these are set out underneath.

Takeovers and mergers play an important role in developing a country's economy.[2] Takeovers and mergers promote good corporate governance by acting as a disciplinary measure against managers who perform poorly, and also promote efficient allocation of resources within companies. Allowing a free market for corporate control is in the best interests of the economy and the society at large.[3] Takeovers should be allowed to occur freely as such transactions pass control of assets and resources to the most productive users.[4] The law should not impede such transfers as these may have huge cost implications for the community and companies may be saddled with

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[1]JF Olson "South Africa moves to a global model of corporate governance but with important national variations" (2010) *Acta Juridica* 219.
[2]See S Deakin "Corporate governance, finance and growth: Unravelling the relationship" (2010) *Acta Juridica* 191.
[3]See D Fischel "Efficient Capital Market Theory, The Market for Corporate Control and Regulation of Cash Tender Offers" (1978) 57:1 *Texas Law Review* 1-2.
[4]MM Katz "Developments in corporate law" (1997) 22:2 *Journal for Juridical Science* 28-41. See also J Mayanja "The equal opportunity principle in Australian takeover law and practice: time for review?" (2000) *Australian Journal of Corporate Law* 15.

poorly-performing directors with no effective way of removing them.[5] Corporate control transactions and subsequent changes in management increase the wealth of investors. Changes to the corporation, such as, the appointment of their own managers, are likely to produce gains for all shareholders but at a lower cost for the new controlling shareholders. In this way, the freedom to undertake a bid encourages bidders to undertake a takeover that, in turn, will benefit all shareholders.[6] The quote below is relevant for the purposes of the mandatory offer:

> "[G]iven its propensity to chill takeover activity and thereby deny shareholders the substantial benefits associated with that activity, it is advisable to reconsider the need for the rule of mandatory equal treatment. While fairness is a laudable objective, the interests of shareholders may be served better by a system of unequal distribution. That system might facilitate more takeover transactions. By ensuring maximum gains from takeover activity, the unequal distribution is likely to enhance the welfare of all shareholders, including shareholders whose shares are not acquired. Society will also benefit to the extent scarce resources are permitted to pass to their optimum uses." [7]

In the words of other scholars:

> "[T]he market for corporate control and threat of cash tender offers are of great importance in creating incentives for management to maximise welfare of shareholders … Since a successful takeover bid results in displacement of current managers, managers have a strong incentive to operate efficiently and to keep share prices high."[8]

For South Africa, scholars have questioned the application of the mandatory offer rule as far back as 1997, and have pointed out that:

> "[I]t is surely in the public interest that corporate assets should be transferred to the stewardship of good managers. Conversely management of companies must be encouraged to good performance by realisation that neither the corporate laws nor the competition laws of the country will stand in the way of a healthy and thriving takeover-

[5]*See* Mayanja (2000) *Australian Journal of Corporate Law* 15.
[6]F Easterbrook & D Fischel "Corporate Control Transactions" (1982) *The Yale Law Journal* 705.
[7]Mayanja (2000) *Australian Journal of Corporate Law* 16.
[8]Fischel (1978) *Texas Law Review* 9.

> industry. This raises, *inter alia* the question whether the mandatory offer to the minority is not an unhealthy impediment to a vital takeover-industry by making acquisitions of control too expensive. As a matter of common law there is no obligation to make an offer to the minority on the occurrence of a change of control."[9]

Transplanted laws rarely work as expected[10] and therefore policy makers should be careful of a "global template" on corporate governance. This template is often based on selected aspects of American and British law and their customs.[11] It is important to understand the relationship between corporate governance, finance and economic growth when considering the role reforms of company law might play in facilitating sustainable economic development.[12] However, it appears that the effect of enhancing laws to protect shareholders are not as clear cut as originally thought, especially for developing countries. Shareholder rights may be over protected or the laws may not be as effective as in their country of origin. Therefore, the need to bring shareholder oriented legal reforms to promote economic growth in developing countries should be questioned.[13]

Chapter 2 discussed the regulations of takeovers and mergers in the US, in particular, the State of Delaware, which is preferred by large companies as their state of incorporation. The chapter discussed the equal opportunity rule in *Perlman case,* which formed the basis of the mandatory offer rule. Further, it was concluded in this chapter that the courts in Delaware, rather than regulatory bodies, play a leading role in regulating the conduct of directors during takeovers and mergers. The courts have established various standards to assess the conduct of directors during takeovers and mergers. The standards include the business judgment rule, enhanced scrutiny and the entire fairness. The standards are intended to protect shareholders during a takeover or merger. The conduct of directors is tested against these standards.

In chapter 3 it was indicated that the development of the regulatory framework for takeover and mergers occurred to protect minority shareholders during takeover bids.

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[9] Katz (1997) *Journal for Juridical Science* 37.
[10] Deakin (2010) *Acta Juridica* 216
[11] See Deakin (2010) *Acta Juridica* 216.
[12] Deakin (2010) *Acta Juridica* 217.
[13] Deakin (2010) *Acta Juridica* 216-217.

The mandatory offer in the UK developed over a fairly long period. In this chapter, it was shown that the application of the mandatory offer rule in the UK is not without concerns. In the EU, the mandatory offer rule has also raised a number of ongoing debates and is not universally accepted. Continuous review of the rule is required, probably to suit various countries' markets for corporate control environment.

The discussion in chapter 4 focused on Australia's unique takeover regulation process applying the Eggleston Principles. The study concluded that Australia does not have a mandatory offer rule despite the fact that its company laws have a close connection with the UK company law. Some academics have suggested that Australia is one of the few countries that addresses the social aspects of takeover in its take-over laws.[14] As appears from the research, Australia adopted a regulatory regime for takeover and merger regulation that does not include the UK mandatory offer rule, in order to suit its economy and financial markets.

In chapter 5, the dissertation investigated the history of regulating takeovers and mergers in South Africa. Various methods of undertaking a merger or a takeover and the regulations applicable to each were discussed. The study found that, while the Takeover Provisions in the Companies Act 2008 have introduced efficient methods for achieving takeovers, teething problems in respect of some of the interpretations and application remain. While the main focus of the dissertation is the mandatory offer in section 123, the study found that practitioners generally welcomed the improved and simplified takeover and merger provisions such as the amalgamation in terms of section 113, scheme of arrangements in terms of section 114, and the voting procedures in terms of section 115. Further, the additional protection for shareholders in the form of appraisal rights in section 164 has also been welcomed despite some problems such as its complexity. It is argued that additional protection such as the detailed disclosures requirements in the regulations, goes a long way to providing sufficient protection of minority shareholders during takeovers and mergers. This further strengthens the position of minority shareholders in takeovers. Some of the provisions regarding protections could be improved and clarified to strengthen the

[14]See B Sheehy "Australia's Eggleston principles in takeover law: Social and economic sense?" (2004) 17 *Australian Journal of Corporate Law*. 2.

protections offered to minority shareholders but once this is achieved minorities will be sufficiently protected even without a mandatory offer requirement. Most importantly, the mandatory offer requirement in section 123, and its role in South African merger regulation is subjected to closer scrutiny and its disadvantages for SA is discussed. The dissertation concludes in chapter 5 that the mandatory offer is not appropriate for South Africa and the reasons are enumerated thereunder.

Chapter 6 provides an evaluation of the takeover and merger regimes of the various comparative countries. These include, the rationale for regulating the transactions, the main institutions regulating those transactions and the methods of dispute resolutions. Several proposals for the strengthening of the institutions and rules relevant to enforcement of takeover rules are made. Most importantly, an evaluation in this chapter shows that academics have criticised the negative impact of the mandatory offer rule on takeovers and mergers. Its efficacy in protecting minority shareholders has also been questioned. Other scholars have extoled its virtues in protecting investors. From the analysis of the various jurisdictions, it appears that there is no clear consensus on the advantages or disadvantages of the mandatory offer rule. This is not surprising for a number of reasons including the fact that the mandatory offer rule affects each country's shareholders differently depending on whether a country's companies have concentrated shareholding structures or not. However, it appears that the debates are stacked against the application of the mandatory offer rule. Some of the criticism appears to be closely related. Some of the main reasons why scholars oppose the mandatory offer can be summed up as:

- the rationale for the decision in the *Perlman* case, (which has served as a strong trigger for a mandatory offer rule) is not clear.[15] Further there is criticism against the calculation and sharing of the premium as indicated in various paragraphs above, including paragraph 5 6 9 3.[16] A change of control without acquisition of shares present a unique challenge to explain the sharing of a premium of

[15]WD Andrews "The Stockholder's right to equal opportunity in the sale of shares" (1965) 78:3 *Harvard Law Review* 515-516.
[16]See also paragraph 6 5 of chapter 6 dealing with difficulties in justifying payment of a premium in changes of control.

control and the obligation for a mandatory offer bid.[17] The right to sell shares when a change of control occurs has also been questioned;[18]

- it increases the costs of a takeover and therefore, discourages persons from undertaking offers;[19]
- it prevents transfer of assets to the most productive managers and prevents efficient use of capital,[20] as additional payment must be made to other shareholders before a takeover can be implemented.
- it hampers the disciplinary aspect of takeovers and mergers[21] and entrenches directors who perform poorly or do not have the appropriate skills to manage particular assets.[22] This is because under-performing directors are aware that they cannot be removed without the new controller having to make a mandatory offer. The role of takeovers in removing inefficiencies is not often reported by the mass media and the well-documented creation of shareholder value by takeovers is often dismissed as "paper gains".[23]
- the application of the mandatory offer rule in countries whose companies have dispersed shareholdings is not suitable in countries where shareholding is concentrated as the rule may encourage entrenchment of control by block-shareholders. This could be to the detriment of good corporate governance as it discourages change of corporate control. [24]
- for South Africa, it appears that the rule is against the aims of policy makers as published in the DTI 2004 Policy document.[25] Despite weaknesses due to implementation, BBBEE policies have generally been accepted as desirable for SA economy. The mandatory offer rule promotes preservation of existing patterns of share ownership to the detriment of BBBEE policies. As pointed out by researchers, existing legislation has a tendency of promoting and preserving

[17]See Andrews (1965) *Harvard Law Review* 551.
[18]See L Gullifer & J Payne *Corporate Finance Law Principles and Policy* (2011) 615.
[19]See Gullifer & Payne *Corporate Finance Law Principles and Policy* 615.
[20]See Mayanja (2000) *Australian Journal of Corporate Law* 16.
[21]See T Papadopoulos "The mandatory provisions of the EU Takeover Bid Directive and their deficiencies." (2007) *Law and Financial Markets Review* 528 at note 30.
[22]See H Manne "Bring Back the Hostile Takeover" (26 June 2002) *The Wall Street Journal* 2.
[23]See GA Jarrell, JA Brickley & JM Netter "The Market for Corporate Control: The Empirical Evidence Since 1980" 2 :1 *The Journal of Economic Perspectives* (Winter, 1988) 49-68 Available at: http://www.jstor.org/stable/1942739 (Accessed 20-10-2013).
[24]See Deakin (2010) *Acta Juridica* 217.
[25]See DTI 2004 Policy document as discussed in Chapter 1. The policy encourages efficient use of capital and seeks to promote corporate governance, among others.

the *status quo*.[26] The mandatory offer rule disadvantages BBBEE investors because these parties may not be able to acquire management control unless they offer the same price to all other shareholders. To acquire a controlling stake in a JSE-listed company, the costs can be very significant, running into millions or even billions. Accordingly, such parties may not be able to pay the price required to acquire control. To the extent that appraisal rights may be used strategically to defeat BBBEE transactions, it should be criticised to the same extent, as discussed under paragraph 6 9 above.

- According to Davies & Worthington, while the mandatory offer may have advantages in certain countries, the mandatory offer bid "discourages acquisitions by those who would increase the value of the company for the benefit of all shareholders but who are wealth constrained and so cannot raise the finance needed to bid for all the outstanding shares."[27]
- And as indicated in Yeats *et al*,[28] the SAC pointed out that:

> " '[T]he mandatory offer makes financing of a take-over expensive, because the offeror must make an offer for all the voting shares of the offeree company, and not only those that will confer control', and that 'the resultant high cost of take-overs hampers the movement towards black economic empowerment in the South African context; because of the high cost of a take-over, the people/entities that presently have economic power are in a position to further entrench that power, because only they have the means to implement a mandatory offer'. "

In South Africa, there are many situations where the mandatory offer is not applied. This reduces its usefulness as a protective measure. For instance, partial offers under section 125(3) allowing a person who crosses the 35 percent mandatory offer threshold not to make the offer if such a person obtains approval by a simple majority resolution of independent shareholder, as discussed in paragraph 5 6 11 2. Further, in the financial period between 31 March 2011 and 31 March 2017, the scheme of

[26]L Bebchuk & M Roe "Theory of Path Dependence in Corporate Ownership and Governance" (1999) *Discussion Paper No. 26610/99, Harvard Law School.* 3.
[27]Davies & Worthington, *Gower Principles of Modern Company Law* 964.
[28]Yeats JL, de la Harpe RA, Jooste RD, Stoop H, Cassim R, Seligmann J, Kent L, Bradstreet RS, Williams RC, Cassim MF, Swanepoel E, Cassim FHI and Jarvis KA *Commentary on the Companies Act of 2008* App1-91.

arrangement has consistently been the most preferred method to implement a takeover or merger by a large margin.[29] Mandatory offers on the other hand are few and far in between with bidders preferring to obtain a waiver from compliance with the mandatory offer requirements.[30] But these requirements of obtaining approval from shareholders not to make the mandatory offer, further add to unnecessary costs for bidders.

In conclusion, takeover laws should achieve a number of objectives including to: protect stakeholders; enhance investment; and promote the market for corporate control. It is important that takeover laws protect minority shareholders to encourage investment. However, this must be done at the right level to maintain integrity of the market.[31] Small shareholders should be encouraged to invest. Too much protection for shareholders can make takeovers and mergers expensive, difficult to undertake, and create an inefficient takeover or merger environment. In this type of market, potential bidders can be discouraged. This in turn can lead to illiquid markets and increased inefficiencies.[32] Hence, it is suggested in this dissertation that the mandatory offer rule should be amended to suit local economic conditions and the environment for the market for control in SA.

7 2 Recommendations

Developing countries are faced with ever changing societal demands and business environments. New rules must be developed to suit local economic development and meet other societal needs. Taking into consideration the additional methods available for effecting a change of corporate control, it is suggested that there are sufficient protections for minority shareholders in the Companies Act 2008. The deletion of the mandatory offer section in its entirety may also facilitate a market for corporate control in general and promote good corporate governance, in line with the DTI 2004 Policy document. In addition, the amendment should remove one of the obstacles towards

[29]See SA Panel Annual Reports for the years ended 31 March 2011-31 March 2017. Available at: www.//trpanel.co.za. (Accessed 30- 5- 2018).
[30]SA Panel Annual Reports.
[31]See N Boardman “A critical analysis of the new South African takeover laws as proposed under the Companies Act 71 of 2008” (2010) *Acta Juridica* 311-312.
[32]Boardman (2010) *Acta Juridica* 311-312.

promoting transfer of ownership of shares to the previously-disadvantaged individuals. This is also in line with the DTI 2004 Policy document as published.

However, should it be found after research that the repeal of the mandatory offer section in its entirety is not desirable, then it is suggested that the exemption provision in section 119(6),[33] and as alternative, section 123 of the Companies Act be amended to facilitate BBBEE transactions. It may be argued that section 119(6) of the Companies Act of 2008 in its current form may be used to relax the strict application of the mandatory offer rule; this is inappropriate. The provisions of section 119(6) must be limited to those transactions that in their own right meet the tests as set out in that section. In addition, such applications are subject to a number of formalities and payment of the necessary fees, which makes them undesirable. The current exemption provisions are also of general application for affected transactions and not specific enough for BBBEE transactions. Therefore, this may lead to difficulty in justifying their application to BBBEE transactions. A specific exemption provision would also give comfort to funders of BBBEE transactions and avoid uncertainties, as is the case in the Competition Act 89 of 1998.

The Competition Act 89 of 1998 in its preamble acknowledges that the SA economy should be opened to a greater ownership by a greater number of its citizens. The Competition Act 89 of 1998 indicates that:

> “2 The purpose of this Act is to promote and maintain competition in the Republic in order- (f) to promote the greater spread of ownership, in particular to increase the ownership stakes of the previously disadvantaged individuals.”

There is sufficient information to justify and conclude that the mandatory offer rule is indeed *not* suitable for application in South Africa in its current form. It is recommended that this rule be reviewed and amended to suit local economic circumstances. A balance should be maintained between the interests of the shareholders and the

[33]Section 119(6) of the Companies Act is a general provision that empowers the Takeover Regulation Panel to exempt certain takeover or merger transactions. Such transaction may be exempted if there is no potential prejudice to other shareholders; the costs of compliance are disproportional to the value of the transaction and in cases where it is reasonable and justifiable to give the exemption under the circumstances.

promotion of the interests of the broader society and the South African economy. Even in the case of the UK, where the mandatory offer rule has been enforced for many years, various scholars have indicated that the unqualified application of the mandatory offer rule needs some thought. As shown in the dissertation, other countries have designed their company laws to accommodate their country requirements, most notably Australia with its unique requirements and the UK which has a very flexible takeover law despite its statutory nature. In the United States, in particular the State of Delaware, the judiciary plays a pivotal role in regulating takeovers and mergers. The TSC established under section 202 of the Act should play a vital role in adjudicating disputes in takeovers and mergers. Its role and powers should be clarified and enhanced. The regulations should be amended to include the following: Chairperson of the TSC should play an active role once a matter has been referred or parties lodge an appeal. This will allow the TSC to give directions and hear the matter as speedily as possible. Further, as pointed out in chapter 5 8 above, the enforcement role of the TSC should be improved to enhance efficiency. For instance, adopting the enforcement mechanism similar to that of the Financial Services Tribunal created under section 219 of the Financial Sector Regulation Act 9 of 2017, will make the process of enforcement to be effective and efficient.

Based on the above conclusions about mandatory offers, there are good reasons for the South African legislature to amend section 123 of the Companies Act along the lines of the recommendations suggested. For South Africa, it should be noted that, “[O]ptimal corporate law depends on institutional context, and a country's corporate law should evolve as its economy and legal system evolve.”[34]

Accordingly, the following recommendations are made:

1 Deletion of section 123 of the Act and applicable Regulations; or

2. Alternatively, amendment of section 123 of the Act to add the following subsection:

[34]B Black & R Kraakman “A Self –Enforcing Model of Corporate Law” (1996) *Harvard Law Review* 1079.

> "123(6) Notwithstanding the provisions of subsection 123(2) above, this section shall not apply to acquisitions intended to promote the spread of share ownership, in particular to increase the share ownership of historically disadvantaged persons as contemplated in the Broad Based Black Economic Empowerment Act No 53 of 2003 as amended." or

3. Amendment of section 119 of the Act by addition of the following subsection:

> "(7) Despite the provisions of section 123 (1) of the Act, an affected transaction in terms of that section entered into by an offeror or persons acting in concert' with such offeror for the purposes of promoting the greater spread of ownership of securities by the previously disadvantaged individuals in accordance with the Broad-Based Black Economic Empowerment Act 53 of 2003, may be exempted in terms in terms of subsection 6."

4. The dissertation in paragraph 5 12, identifies a number of glaring deficiencies and difficult sections and regulations. It is suggested that these should be rectified so that the Takeover Provisions can better promote some of the objectives set out in section 7 of the Companies Act of 2008.

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