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Share Repurchases, Schemes of Arrangement and the Takeover Regulations

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Since the promulgation of the Companies Act No 71 of 2008 ("**Companies Act**") there has been a debate as to whether or not every repurchase by a company of more than 5% of its own shares constitutes a scheme of arrangement.

The genesis of this debate is the wording of section 48(8)(b) of the Companies Act. That section stipulates that a decision by the board of directors of a company to acquire more than 5% of the company's own shares, whether in one transaction or through a series of integrated transactions ("**Qualifying Repurchase**"), is subject to the requirements of sections 114 and 115 of the Companies Act.

In light of the fact that section 114 of the Companies Act deals with schemes of arrangement, it was argued that a Qualifying Repurchase must automatically to be regarded as a scheme of arrangement.

On 5 February 2021, the Gauteng Division of the High Court, Johannesburg had the opportunity to consider, *inter alia,* this issue in *First National Nominees (Pty) Ltd and others v Capital Appreciation Limited and another* (case no 19/41679).

The Companies Act does not contain a definition of a "scheme of arrangement" so the court was left to consider this question. The court concluded that "*the objective of an arrangement in terms of section 114 [i.e. a scheme of arrangement] is to affect the respective rights and obligations inter se of the company and its holders of securities in a manner which cannot otherwise be conveniently achieved by independent agreement between the company and each holder of securities*". It is apparent that the function of a scheme of arrangement is to provide a mechanism to affect the respective rights and obligations between a company and its shareholders and shareholders *inter se* in circumstances where doing so by a conventional agreement between all of those parties is not an option. Axiomatically, a share repurchase pursuant to an agreement between a company and certain of its shareholders that does not seek to bind other shareholders who have not agreed thereto is not a scheme of arrangement. An arrangement that seeks to bind all shareholders, assuming all of the applicable statutory requirements are met and regardless of whether or not such shareholder/s voted in favour thereof (i.e. agreed thereto), is by its nature a scheme of arrangement.

The court went on to deal with the wording of the section 48(8)(b) of the Companies Act itself stating that wording clearly does not state that the Qualifying Repurchase is a scheme of arrangement, but rather that every Qualifying Repurchase is subject to the requirements set out in sections 114 and 115 of the Companies Act. The court acknowledged that, although a share repurchase may be implemented by means of a scheme of arrangement in terms of section 114 of the Companies Act, not every Qualifying Repurchase automatically falls to be classified as such. A Qualifying Repurchase is not to be regarded as a scheme of arrangement solely by virtue of the need to comply with the wording of section 48(8)(b) of the Companies Act. A Qualifying Repurchase that is not intrinsically of the nature of a scheme of arrangement is no more than a share buy-back subject to the further conditions found in sections 114 and 115 of the Companies Act. A Qualifying Repurchase will only be a scheme of arrangement if, by its nature, it seeks to bind all shareholders whether they agree thereto or not.

According to the court, the rationale behind the application of the additional requirements to Qualifying Repurchases is that "*such transactions merit additional protection because they potentially affect minority shareholders more radically as they amount to a restructuring of the shares of the company*". It was the view of the court that the legislature accordingly saw it fit to impose on Qualifying

Repurchases the protections that are already contained in sections 114 and 115 of the Companies Act and not to render all Qualifying Repurchases as schemes of arrangement.

The additional requirements applicable to Qualifying Repurchases include, *inter alia*, the appointment of an independent expert as contemplated in section 114(2), the adoption of a special resolution as contemplated in section 115(2)(a) and, importantly, the entitlement for shareholders to exercise appraisal rights in terms of section 115(8) (read with section 164) of the Companies Act. The purpose of the legislature in making the additional requirements applicable to Qualifying Repurchases was not to convert a simple share buy-back contemplated in section 48 of the Companies Act into a scheme of arrangement, but rather to protect shareholders against potential abuses that could accompany Qualifying Repurchases.

Furthermore, although not expressly considered by the court, the judgment arguably provides clarity on an additional aspect, namely whether a Qualifying Repurchase constitutes an "affected transaction" which is subject to the Takeover Regulations. Since there was a view that a Qualifying Repurchase is a scheme of arrangement, Qualifying Repurchases were therefore considered "affected transactions" by virtue of section 117(c)(iii) of the Companies Act, which states that an affected transaction means "*a scheme of arrangement between a regulated company and its shareholders, as contemplated in section 114, subject to section 118(3)*". Accordingly, since the court has ruled that Qualifying Repurchases are not always schemes of arrangement, it seems only logical that a Qualifying Repurchase will not constitute an "affected transaction" unless it is a scheme of arrangement by nature.

In conclusion, a Qualifying Repurchase, which is not a scheme of arrangement will therefore not be subject to the Takeover Regulations. It should, however, be noted that the implementation of a Qualifying Repurchase may give rise to a different kind of affected transaction such as a mandatory offer or a comparable offer.

It remains to be seen whether this judgment will be appealed.

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