

Shareholder “divorce” – is dissolution of the company a viable remedy?

3 March 2021 6 min read

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It occurs in practice that relationships between shareholders in small private companies may breakdown over time when material differences arise between them. In these circumstances the question may arise as to whether a disgruntled shareholder could “divorce” itself from such company and the other shareholders, notwithstanding that the company is solvent and functioning. In this regard, a potential remedy to achieve such a “divorce” may lie in section 81(1)(d)(iii) of the Companies Act, 71 of 2008 (“**Act**”) which provides *inter alia* that a court may order the winding-up of a *solvent* company on application by a shareholder on the ground that it would be ‘*just and equitable*’ for the company to be wound up.

This article briefly discusses the considerations which South African courts may take into account in determining when it would be ‘just and equitable’ to order that a solvent company be wound up.^[1]

The importance of trust and confidence amongst shareholders

It is generally accepted that a complete deadlock amongst shareholders (i.e. in voting power), which has the effect of paralysing the operation of a company could be a valid ground which a shareholder may rely on in order to apply for the winding-up of the company.

However, the application of the ‘deadlock principle’ which is contemplated in section 81(1)(d)(iii) of the Act is in practice not as clear-cut. This subsection may provide a remedy, such as the winding-up of a company, where there has been a complete breakdown in ‘*trust and confidence*’ amongst shareholders. This can occur where a relationship exists between shareholders which is particularly personal, similar to the relationship which exists between partners in a partnership.

It is therefore clear that an actual deadlock is not essential and that, what is necessary is to satisfy the court that it has become impossible for the aggrieved shareholder to place the requisite ‘trust and confidence’ in the other shareholder/s, because such other shareholder/s have breached an underlying partnership-type arrangement or understanding that existed between the shareholders (whether express, tacit or implied).

A viable remedy notwithstanding the lawful exercise of rights by the board or shareholders?

Where a company is being lawfully administered by its board and/or shareholders in accordance with the company’s constitutional documents, and there is no underlying partnership-type arrangement or understanding which exists, the courts will not necessarily permit a dissatisfied shareholder to “*escape from what is merely an unhappy investment*”^[2].

However, where an underlying partnership-type relationship does exist and conduct by the directors or shareholders of a company constitutes a lawful exercise of rights or powers, but is nevertheless at odds with that which was in the contemplation of the parties when they became shareholders of the company, it may be that the courts would allow an aggrieved shareholder to escape from the company. In this regard, we quote precisely the following elegantly summarised principle:

*The court will not ignore the rights and obligations conferred by company law and the company's articles. **But what is a valid exercise of such rights may nevertheless be entirely outside what can fairly be regarded as having been in the contemplation of the parties when they became members of the company and the courts will therefore subject their exercise to equitable considerations of a personal character.** Thus, the just and equitable ground enables the court **'to subject the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way.'**^[3]*

Accordingly, where a partnership-type relationship exists between shareholders and subsequently breaks down, notwithstanding that a company's affairs are being lawfully administered and may even be profitable, that company could be wound up by an aggrieved shareholder on the ground that it would be just and equitable to do so taking into consideration the complete breakdown in 'trust and confidence' amongst its shareholders due to a breach of the understanding and expectation between the shareholders, which did not contemplate such conduct and state of affairs.

Clean-hands

Whilst it should be noted that a court will not usually order the winding-up of a company sought by a shareholder who approaches the court with 'unclean hands' (i.e. where the shareholder is guilty of some form of misconduct or is otherwise partly responsible for the breakdown of the relationship), the courts have stated that the 'unclean hands' would not necessarily preclude relief under section 81(1)(d)(iii). A court will ultimately consider the respective contributions of each party to the breakdown of the relationship.

This remedy should be a last resort

Winding up of a company will only be granted by a court as a last resort, where there are no alternative remedies. In this regard, an alternative remedy may be found in section 163 of the Act which provides a remedy to a shareholder where the company is being, or has been, carried on or conducted in a manner that is oppressive or unfairly prejudicial to the shareholder and which section grants the court a wide discretion to make any order which it deems fit.

The courts have also taken into consideration, in the context of section 163, factual circumstances which indicate that a company is being administered lawfully and within the powers of the relevant directors or shareholders, but which is unfairly prejudicial to a shareholder, and have stated that where powers have been exercised in accordance with a company's constitutional documents, a court should be wary of substituting its own business judgment for that of the persons entrusted with that decision. It may therefore be that section 163 would not provide an alternative remedy where rights have been lawfully exercised, and that section 81(1)(d)(ii) would be a viable remedy and as a last resort.

Whilst this article briefly considers certain of the considerations which have been dealt with by courts in the context of section 81(1)(d)(iii) of the Act, it should be noted that the legal issues relevant to this section are complex and require proper legal consideration within the context of the particular set of facts of the company concerned.

[1] *Inter alia* Thunder Cats Investments 92 (Pty) Ltd v Nkonjane Economic Prospecting Investment (Pty) Ltd 2014 5 SA 1 (SCA); Erasmus v Pentamed Investments (Pty) Ltd 1982 (1) SA 178 (W); Cilliers NO and Others v Duin & See (Pty) Ltd 2012 (4) SA 203 (WCC); Apco Africa (Pty) Ltd and Another v Apco Worldwide Inc 2008 (5) SA 615 (SCA); Budge and Others NNO v Midnight Storm Investments 256 (Pty) Ltd and Another 2012 (2) SA 28 (GSJ)

[2] Commentary on the Companies Act (2012) Blackman, Jooste, Everingham, Cassim, de la Harpe, Larkin, Rademeyer, Yeats page 106.



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