



CORPORATE MERGERS & ACQUISITIONS

The Balancing Act: The Sharing of Company Information by Exiting Shareholders with Potential Third-Party Purchasers

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and Emma Reid, Candidate Attorney

1. INTRODUCTION

The default position regarding who can access a company's records and information ("**company information**") and the nature and extent of what company information a person may access is set out in section 26 of the Companies Act, 71 of 2008 ("**the Companies Act**").

When a shareholder wishes to sell its shares in a company, it will typically need to put in place a sale process (either directly with a preferred purchaser or potentially in the form of a competitive bid process). As part of such sale process, a preferred purchaser or the competitive bidders ("**third-party purchaser**") would need to undertake a due diligence process in respect of the company in question in order to determine whether they wish to acquire the shareholder's equity interest in the company, and at what price and on what terms and conditions.

In order to undertake such a due diligence process, the shareholder would need to provide the third-party purchaser with various information and documentation pertaining to the company including, but not limited to, its financial position, financial performance, its business operations, employees, intellectual property, contractual relationships, regulatory compliance, tax affairs, and other matters.

It may, however, be the case that the memorandum of incorporation ("**MOI**") and / or the shareholders agreement ("**SHA**") in respect of a company to impose confidentiality undertakings on shareholders which may prohibit them from disclosing, or which may limit the extent of disclosure, to third-party purchasers of certain of the types of information described above.

Furthermore, the scope of company information which is accessible to external parties (i.e. non-shareholders and non-directors), such as third-party purchasers, in terms of section 26(2) of the Companies Act is very limited. The reason for this is that the Act seeks to prevent access to sensitive company information by persons who may not have a legitimate interest in such information.

This has the potential to create a conundrum for shareholders who wish to exit their investment in a private company, because they may find themselves in a situation where they do not have clear rights under the MOI or SHA of the company to disclose certain company information to third-party purchasers to enable them to conduct a due diligence on the company, and/or may be unable to reach agreement with the board of directors of the company and/or the other shareholders of the company on what types of company information may be disclosed to third-party purchasers, and under what conditions such disclosure may be made by the shareholder. Such a scenario could hinder a shareholder's ability to provide a third-party purchaser with all of the information and documentation which the third-party purchaser has requested in respect of the company for it to conduct a due diligence on the company to its satisfaction.

This article briefly sets out the position under section 26 of the Companies Act, and examines how shareholders and companies may seek to balance the requirement of shareholders to disclose company information to third-party purchasers, on the one hand, with the requirement of companies to effectively protect the confidentiality of company information on the other hand.

2. SECTION 26 OF THE COMPANIES ACT: THE DEFAULT POSITION

2.1. Shareholders' information rights

Section 26(1) of the Companies Act (read with section 24 of the Companies Act) grants shareholders of a company the right to inspect the company's MOI (as well as any amendments, alterations or rules thereto), the directors' records, the securities register of the company, the annual financial statements of the company, any reports presented at an annual general meeting of the company, the notices and minutes of all shareholders meetings, including all resolutions adopted by the shareholders and any document that was made available by the company to the shareholders in relation to each such resolution, and copies of any written communications sent generally by the company to all shareholders.

Whilst section 26(1) would enable a shareholder to obtain such types of information from the company, it should be noted that section 26(1) does not specify how such a shareholder may utilise such information. It may be arguable whether a shareholder is permitted to disclose all such information to a third-party purchaser, either by virtue of confidentiality undertakings which may be contained in a company's MOI or SHA, or by virtue of certain of such information being confidential to the extent that the company may be able to prove this on some or other legal basis.

2.2. Any other person's information rights

In terms of section 26(2) of the Companies Act, any other person (including a potential third-party purchaser) only has a right to inspect the company's securities register and the company's register of directors.

Consequently, if a third-party purchaser's ability to access company information is limited to the types of information contemplated in section 26(2) of the Companies Act, such a third-party purchaser would find themselves with very little useful information concerning the company for purposes of conducting a due diligence.

2.3. The establishment of additional information rights in a company's MOI

Section 26(3) of the Companies Act expressly allows for a company's MOI to establish additional information rights (with respect to company information) for any person or categories of person as long as such additional rights do not negate or diminish the mandatory protection of any record as afforded by the Promotion of Access to Information Act, 2 of 2000 ("PAIA").

In this regard, section 68 of PAIA stipulates that a request for company information may be refused by the company if the information requested includes (i) trade secrets of the company, (ii) financial, commercial, scientific or technical information, other than trade secrets, of the company, the disclosure of which would be likely to cause harm to the commercial or financial interests of the company, (iii) information, the disclosure of which could reasonably be expected to put the company at a disadvantage in contractual or other negotiations and/or prejudice the company in commercial competition.

Whilst section 26(3) of the Companies Act clearly permits the establishment of additional information rights in a company's MOI in favour of third parties which could include a third-party purchaser, the effect of section 68 of PAIA would largely negate the effectiveness of including such additional information rights in the MOI of a company.

In any event, it is doubtful whether the board or shareholders of a company would want to provide in its MOI for any person or categories of person to have access to the abovementioned types of company information in terms of a general right which may be enforced by a person or categories of person, but would likely prefer to instead grant shareholders the right to access and disclose certain types of company information to potential third-party purchasers who such shareholders are engaging with in the context of a sale process, subject to certain requirements being complied with by such shareholder and third-party purchaser.

3. REGULATING THE DISCLOSURE OF COMPANY INFORMATION BY A SHAREHOLDER TO THIRD-PARTY PURCHASERS

Having regard to the abovementioned considerations, a practical solution which would allow a shareholder to disclose company information to a third-party purchaser whilst effectively protecting the confidentiality of company information is to, at the time that the investor acquires its shareholding in the company, require that the company's MOI or the SHA includes provisions which provide that –

- shareholders shall have the right to request and receive from the board of the company certain agreed upon types of company information (the nature and extent of which should be described in the MOI or SHA in adequate detail) which would typically be requested by a third-party purchaser to conduct a legal, financial and tax due diligence on the company, for the purpose of a shareholder sharing such company information with a third-party purchaser, which is not a competitor of the company, as part of a sale process being conducted by a shareholder;
- the provision of such agreed upon company information to the shareholder for purposes of the shareholder sharing same with the third-party purchaser shall be subject to –
 - a. prior written notification by the shareholder to the company regarding the identity of the third-party purchaser so as to enable the board of the company to satisfy itself that the third-party purchaser is not a competitor of the company; and
 - b. the conclusion of a written non-disclosure agreement between the third-party purchaser and the company, the terms of which shall be to the reasonable satisfaction of the board of the company.

4. CONCLUSION

As noted above, section 26 of the Companies Act is not likely to provide shareholders with the necessary information rights and the right to disclose company information to third-party purchasers which would enable shareholders and third-party purchasers to effectively conduct a due diligence process.

It is therefore suggested that investors negotiate the inclusion of appropriate information rights and disclosure rights in the MOI or SHA of a private company at the time of making their investment in such company. The inclusion of provisions of the kind described in section 4 of this article would arguably help to achieve a balance between the requirement of a shareholder

to be able to access and disclose company information to third-party purchasers as part of a sale process with the requirement of a company to be able to maintain the confidentiality of its proprietary and competitively sensitive information.

It is recommended that shareholders and companies should obtain advice from commercial attorneys who have the necessary expertise to advise on these matters.



Jarryd Mardon

Director

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Francisca Heese

Associate

[View Profile](#)