

The pride or prejudice of being a related person to a company?

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Introduction

In terms of Section 163 of the Companies Act 71 of 2008 (**"the Act"**), shareholders or directors of a company ("applicant") are afforded several instances to apply to the court for relief in terms of section 163 of the Act. One such instance is where an act or omission of a related person^[1] of the company, has had a result that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant.

It is not uncommon for a business opportunity to present itself which requires that the resources and expertise of more than one entity are pooled together in order to procure and successfully execute the business opportunity. An example of this is where national, provincial or local government publish a request for tender submissions requesting that interested and eligible businesses submit a tender application that complies with the requirements described in the request for tender submissions.

It is often that the scope of works as described in the request for tender submissions span across several specialized areas of expertise. A further factor that is taken into consideration in the awarding of such tenders is the tenderors' compliance status under the Broad-Based Black Economic Empowerment (**"B-BBEE"**) legislation.

For purposes of complying with the tender requirements, the relevant companies who are interested in the tender may elect to incorporate a joint venture company to operate as a special purpose vehicle (**"JV Company"**) in which they pool their resources and which they agree will act as the tenderor.

It is likely that one of the companies that will be a shareholder of the JV Company will serve as the black economic empowerment partner (**"B-BBEE partner"**) by virtue of its favourable B-BBEE status, in addition to the other assets, services or capital which the B-BBEE partner contributes to the JV Company.

For the purposes of this article, the following scenario is assumed to exist. The B-BBEE partner holds 51% of the issued shares in the JV Company. The B-BBEE partner happens to be a wholly-owned subsidiary of a 100% black-owned company (**"the Holding Company"**) ie the Holding Company holds 100% of the issued shares in the B-BBEE partner.

It is also understood that the Holding Company co-operated with the other shareholders in the JV Company and put forward the B-BBEE partner as its chosen entity which will hold its shareholding in the JV Company.

In these circumstances, the Holding Company would be deemed to be a related person to the JV Company by virtue of the fact that it indirectly controls the majority of the voting rights of the shares in the JV Company through its wholly-owned subsidiary (ie the B-BBEE partner).

For purposes of this scenario, it is pointed out that following the successful award of the tender to the JV Company, the other shareholders of the JV Company become aware of the fact that the Holding Company has subsequently sold a significant portion of its shares in the B-BBEE partner to a third party (which has a considerably lower B-BBEE status than the Holding Company) without consultation with the other shareholders of the JV Company (**"the Sale"**).

Cause of complaint

A complaint may arise regarding the Sale if, for instance, it was understood amongst all the shareholders of the JV Company that the B-BBEE partner would maintain its B-BBEE status for purposes of complying with the tender requirements (as derived by it from its 100% holding company (ie the Holding Company), and where this was an integral term and arrangement upon which all the shareholders had agreed to become shareholders in the JV Company.

Accordingly, where the identity of the third party to whom the Holding Company has sold a significant portion of its shares in the B-BBEE partner has a consequential detrimental effect on the B-BBEE status of the B-BBEE partner and consequently also the B-BBEE status of the JV Company, which leads to a breach by the JV Company of the tender conditions, the remaining shareholders of the JV Company (“Aggrieved Shareholders”) may be exposed to serious business risks in connection with their investment in the JV Company.

In such instance, it may be arguable that the conduct of the Holding Company as a related person to the JV Company (because of its status as an indirect holding company of the JV Company), has or had a result that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of the Aggrieved Shareholders.

Potential Remedy

In the circumstances, the Aggrieved Shareholders may potentially be able to apply to a court for relief in terms of section 163 of the Act, as follows –

- 1. directing that the Holding Company, as a related person to the JV Company, restore the Aggrieved Shareholders any part of the consideration that the Aggrieved Shareholders contributed in exchange for shares in the JV Company, with or without conditions as envisaged in section 163(2)(g) of the Act; and/or
- 2. directing that the Holding Company, as a related person to the JV Company, pay compensation to the Aggrieved Shareholders, as envisaged in section 163(2)(j) of the Act, for any losses suffered by the arising from the breach of the tender conditions.

Conclusion

In the instance where an applicant seeks to rely on section 163 of the Act to seek relief from the prejudicial conduct of a related person to a company, the above example illustrates that there is likely to be complex circumstances which will need to be considered with the assistance of professional legal advice.

[1] The term “related person” is defined in the Act to include, amongst others, where one company (ie a holding company) directly or indirectly controls 100% of the voting rights in another company (ie a subsidiary).



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