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Transfer and liquidation:

A critical analysis of the transfer of shares during the process of liquidation and an analysis of Sections 8(2)(b), 15(6) and schedule 5 of the Companies Act 71 of 2008

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DECLARATION

I, **Nicole Anthea Pape**, declare that

'***Transfer and liquidation:***

A critical analysis of the transfer of shares during the process of liquidation and an analysis of Sections 8(2)(b), 15(6) and schedule 5 of the Companies Act 71 of 2008'

is my own work and that it has not been submitted before for any degree or examination in any other university, and that all sources I have used or quoted have been indicated and acknowledged as complete references.

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_____2018

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_____2018

ABSTRACT

Transfer and liquidation: A critical analysis of Sections 8(2)(b), 15(6) and schedule 5 of the Companies Act 71 of 2008.

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LLM Thesis, Department of Mercantile and Labour Law, University of the Western Cape

In corporate law, the transfer of shares plays an important role and until the case of *Smuts v Booyens; Markplaas (Edms) Bpk v Booyens* 2001 (4) SA [SCA] courts were not always clear on the meaning of 'transfer'. What constitutes a transfer of shares and the juncture at which the law regards that transfer as having taken effect is therefore of critical importance where an insolvent company is being wound-up.

The objective of this study is to provide a thorough analysis of the restrictions and limitations imposed on the transfer of shares of a private company being wound-up or any alteration in the status of its shareholders effected after the commencement of the winding-up. The position on transferability of shares is one of the defining features of a private company, in order to exist as a private company, it has to provide such restrictions as it deems fit by way of its Memorandum of Incorporation.

This thesis focuses on the problems pertinent to the transfer of shares of a company being wound-up by looking at the relevant sections of the Companies Act, cases and experiences from other jurisdictions in the hope that it will provide some kind of recourse to the plight of a purchaser who finds himself in the position where he has been made owner of the shares by means of cession but not the shareholder for the purposes of enforcing the right against the

company. With any luck this study will capture the attention of academics and judges alike, so that those in a position to do so will re-consider its strength and validity.

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LIST OF ABBREVIATIONS

Companies Act 71 of 2008	Act / New Act
Companies Act 61 of 1973	Old Act
Constitution of the Republic of South Africa, 1996	Constitution
The Companies and Intellectual Properties Commission	the commission
United Kingdom	UK
South Africa	SA
Articles of Association	AOA
Memorandum of Incorporation	MOI
Supreme Court	SC
Australian Securities and Investment Commission	ASIC
Saad Investment Co. Ltd	SICL

KEY WORDS AND PHRASES

Companies Act 61 of 1973

Companies Act 71 of 2008

Insolvency Act 24 of 1936

King III Code

King IV Code

Corporate Law Reform Policy

Company

Directors

Shareholders

Transferability

Securities / shares

Winding-up

Restriction

Cession

Delivery

Registration

Beneficial owner

Pre-emptory rights

Pactum de non cedendo

TABLE OF CONTENTS

4. CHAPTER FOUR

THE TRANSFER OF SHARES DURINGH THE PROCESS OF LIQUIDATION: AN ANALYSIS OF THE EXPERIENCES IN AUSTRALIA AND THE UNITED KINGDOM

5. CHAPTER FIVE

CONCLUSION, FINDINGS AND RECOMMENDATIONS

CHAPTER ONE

1.1 INTRODUCTION AND BACKGROUND TO THE STUDY

This chapter offers a background, research problem, purpose objective and significance of the study. In addition, it offers methodology, limitations, proposed structure to the study.

The Companies Act 71 of 2008 (the Act) superseded the Companies Act 61 of 1973 (the Old Act), Companies Amendment Act 3 of 2011 together with the Companies Regulations, 2011 and the Close Corporations Act of 1984 as amended by and provided for in Schedule 5 of the Act.[1] Together with the King III Code, it is the most fundamental amendment of company law in thirty years.[2] The Code was further amended by the introduction of the new King IV Code, and like its predecessors, it focuses on the concept of stakeholder inclusivity and emphasises that companies are not only responsible for the economic bottom line but critically need to consider the societal and environmental impacts and outcomes of their operations.[3]

The Act was enacted against the backdrop of a general Corporate Reform Policy published by the Department of Trade and Industry in 2004, the aim of which was to provide a viable alternative to the formalised, bulky and outdated Old Act of 1973. Due to the changes in the global and domestic environments and the changes in local expectations and standards there was a need for a new regulatory framework of corporate activity. There were millions of entities

[1] Smith Tabata Buchanan Boyes 'Guide to Companies Act NO 71 of 2008' available at *https://www.stbb.co.za/wp-content/uploads/2014/09/Guide_to_Companies_Act_2011.pdf* (accessed 28 July 2017).

[2] Smith Tabata Buchanan Boyes 'Guide to Companies Act NO 71 of 2008' available at *https://www.stbb.co.za/wp-content/uploads/2014/09/Guide_to_Companies_Act_2011.pdf* (accessed 28 July 2017).

[3] Pwc 'King IV Code brings the role of ethical and effective leadership to the fore' available at *http://www.pwc.co.za/en/press-room/king-four-draft.html* (accessed 7 September 2017),

active in the economy some of which were informal and unregistered and thus the primary focus of the Act was to encourage unregistered entities into the formal economy to be in line with government objectives and to bridge the gap between first and second economies.[4]

It is driven by both our new democratic dispensation and the pace of change in the global economy.[5] The purposes of the Act and the King Code were to nurture compliance with the Bill of Rights as provided for in the Constitution of the Republic of South Africa, 1996 (the Constitution).[6] It was perceived that this approach in company law would encourage high standards of corporate governance and provide for balancing of rights and obligations of shareholders and directors.[7]

The corporate law reform policy specifically speaks about the transfer of shares and liquidation of companies. Particular attention should be given within the context of changes to the law of corporate insolvency and to the role and responsibilities of liquidators in the process of winding-up and their powers of inquiry.[8] Simplification and streamlining is necessary when considering the duties imposed on liquidators in the current company and insolvency law.[9] Thus it is important that consideration be given to the need for statutory recognition of the

[4] Smith Tabata Buchanan Boyes 'Guide to Companies Act NO 71 of 2008' available at *https://www.stbb.co.za/wp-content/uploads/2014/09/Guide_to_Companies_Act_2011.pdf* (accessed 28 July 2017).

[5] Mphlwa M 'South African Company Law for the 21st Century: Guidelines for Company Law Reform' available at *www.turnaround-sa.com/pdf/GuidelinesforCorporate.pdf (accessed on 11 August 2017).*

[6] The Constitution of the Republic of South Africa, 1996 (the Constitution).

[7] Smith Tabata Buchanan Boyes 'Guide to Companies Act NO 71 of 2008' available at *https://www.stbb.co.za/wp-content/uploads/2014/09/Guide_to_Companies_Act_2011.pdf* (accessed 28 July 2017).

[8] Department of Trade and Industry 'South African Company Law for the 21st Century: Guidelines for Company Law Reform' available at *www.turnaround-sa.com/pdf/GuidelinesforCorporate.pdf (accessed on 11 August 2017).*

[9] Department of Trade and Industry 'South African Company Law for the 21st Century: Guidelines for Company Law Reform' available at *www.turnaround-sa.com/pdf/GuidelinesforCorporate.pdf (accessed on 11 August 2017).*

requirements for being a liquidator and these provisions should not be used to subvert the interests of creditors and other stakeholders such as new owners of company securities.[10]

This thesis will explore the meaning of the transfer of shares in terms of the common law, the Old Act and the Act, as well as how the courts view what transfer is today. In particular, it will critically analyse various sections and schedule 5 of the Act with regard to the transfer of securities in the course of a liquidation process of a company. It will question the recourse that a purchaser has in such an instance and will draw on experiences from other jurisdictions to develop a possible solution to this problem.

1.1.1 Shares and Transfer

The transfer of shares is the process of changing ownership of shares from one shareholder to another. Even though personal rights [like a share] are transferred in ownership through cession, simply ceding the shares does not make the new owner a shareholder. There is a series of steps which have to be followed one of which is the registration of the new shareholder in the company's securities register.[11] Even though this is a standard operation it does require considerable attention to be executed properly, given its importance.

1.1.2 Insolvency / Liquidation

The Insolvency Act 24 of 1936 (the Insolvency Act) in terms of section 2 expressly excludes a company from the procedure of the Act. Companies are liquidated under the law relating to

[10] Department of Trade and Industry 'South African Company Law for the 21st Century: Guidelines for Company Law Reform' available at *www.turnaround-sa.com/pdf/GuidelinesforCorporate.pdf (accessed on 11 August 2017).*

[11] The Companies Act 71 of 2008, s35(1)*(ii).*

companies.[12] This means that the estate of a company is not sequestrated but is wound-up instead. Winding-up refers to the procedure by which a company's assets are sold, debts are paid and if there is any money left it is divided amongst the shareholders according to their rights. Once a company has been wound up, the Companies and Intellectual Property Commission (the Commission) records that the company has been dissolved and publishes a notice to this effect. The company is then terminated. The winding-up process is regulated by sections 79-81 of the Act however these provisions deal with the winding-up of solvent companies. Chapter XIV (sections 337-426) of the Old Act, with certain exceptions, continues to apply to the winding-up and liquidation of companies as though the Old Act had not been repealed.[13]

1.2 RESEARCH PROBLEM

If a transfer is executed after commencement of the process of winding-up, a purchaser's right to the shares is left to a discretionary decision made by the liquidator.[14] This affects the purchaser's rights to property under the Bill of Rights, and a breach of the company's obligations under the contract by the company / liquidator.

Section 341(1) of the 1973 Companies Act provides the following - [15]

[12] Insolvency Act 24 of 1936, s 2; Sharrock R, Van der Linde K, Smith A *Hockley's Insolvency Law* 9 ed (2014) 240.

[13] Sharrock R, Van der Linde K, Smith A *Hockley's* (2014) 240.

[14] The Companies Act 61 of 1973, s 341(1); Schedule 5 of the Companies Act 71 of 2008; The transitional arrangements of the Companies Act 2008 (as set out in Schedule 5 to the Act) provide that in relation to the winding up of insolvent companies Chapter XIV of the now-repealed Companies Act 1973 remains in force. Included in Chapter XIV of the new Act is section 341 of the Old Act.

[15] Schedule 5 of the Companies Act 71 of 2008.

(1) "Every transfer of shares of a company being wound-up or alteration in the status of its members effected after the commencement of the winding-up without the sanction of the liquidator, shall be void."[16]

An interpretation of this provision requires one to determine what constitutes a transfer of a share and at what point the law regards this transfer to be effective during the winding-up of an insolvent company.[17] The interpretation of section 341(1) depends entirely on what should be understood under transfer because when section 341(1) refers to the transfer of shares the interpretation of the word 'transfer' impacts greatly on the person to whom shares are transferred.

Section 341(1) makes it clear that every transfer of shares that occurs at the starting point of the winding-up of a company is void. The section also confirms that the liquidator has a discretion and authority to permit otherwise.[18] This is an indication that the liquidator can make a decision that the transfer is not void. This, in turn, brings up issues of the scope of discretion of a liquidator.

It is therefore critical to determine at what time transfer takes place; is it at the moment where there is consensus between the parties, after cession or after registration has taken place in the company's security register? This question presents a crucial issue in light of section 341(1) and the winding-up of a company on the grounds of its insolvency. Consequently, this study seeks to establish the effect of the nexus between the insolvency on one hand, and the transfer of shares on the other hand.

[16] The Companies Act 61 of 1973, s 341(1)
[17] The Companies Act 61 of 1973, s 341.
[18] The Companies Act 61 of 1973, s 341(1).

If the transfer of the share occurred before the winding-up of a company begins then the transfer is not void in terms of section 341(1) but if the transfer occurred after the commencement of the winding-up, it is void unless the liquidator decides that it is not void.[19] It is therefore an important issue to determine the meaning of transfer in the context of section 341.

While the Act is silent on this point, in *Inland Property Development Corporation (Pty) Ltd v Cilliers,*[20] the court held that:

> 'In regard to shares, the word 'transfer', in its full and technical sense, is not a single act but consists of a series of steps, namely an agreement to transfer, the execution of a deed of transfer and, finally, the registration of the transfer. As was put by Lord REID in the House of Lords in *Lyle and Scott Ltd. v Scott's Trustees and British Investment Trust Ltd., 1959 A.C. 763.*[21]

As such this interpretation would mean that where a company's shares are sold and the company subsequently is wound-up on the grounds of insolvency before the shares are registered in the company's securities register in the name of the person who acquired the shares, the transfer in question would be void in terms of section 341(1) unless the liquidator decides otherwise.[22] If this is correct, the question then becomes what recourse the purchaser

[19] The Companies Act 61 of 1973, s 341(1).
[20] 1973 (3) SA 245 (A).
[21] *Inland Property Development Corporation (Pty) Ltd v Cilliers* 1973 (3) SA 245 (A) para 16; Lyle and Scott Ltd. v Scott's Trustees and British Investment Trust Ltd., 1959 A.C. 763 ('a case which dealt with the word 'transfer' in the articles of association of a company) 778'.
[22] The Companies Act 61 of 1973, section 341(1); *Inland Property Development Corporation* para 16.

has, as clearly a valid contract between the purchaser and the seller of the shares came into existence as both parties performed their duties?[23]

While the transfer of shares plays an important role in corporate law, the courts were never clear on the meaning of transfer before *Smuts v Booyens*[24]. The court held that despite the fact that a cession of the shares would hold the cessionary the owner of the share, he will not be regarded as a shareholder for the purposes of enforcing the right against the company.[25] The owner thus becomes a beneficiary owner of the share whilst the cedent continues to hold the title of shareholder, in other words, a nominee shareholder, who may still vote at meetings and who is still entitled to qualify for a dividend.[26] Thus in order for the cessionary to obtain these rights and become the shareholder the other steps of 'transfer' must be followed i.e. registration in the company's share register.

In terms of section 15(6) of the Act the Memorandum of Incorporation (MOI) constitutes an agreement between the shareholders *inter se*[27] which means that exactly the same reservations that were offered in *Smuts v Booyens* relating to the Articles of Association (AOA) will find application. Consequently, the relationship between shareholders is no different now from the time of *Smuts v Booyens* and the impact of the provisions of section 341 still remains. As such the plight of the shareholder will be precisely the same now in insolvency situations as it was then. There seems to be no remedy for a shareholder to whom shares have been transferred unless transfer took place before the winding-up process started. The interpretation of transfer

[23] Hutchison, Pretorius & Du Plessis 'et al' *The Law of Contract in South Africa* 2 ed (2012) 6.
[24] *Smuts v Booyens; Markplaas (Edms) Bpk v Booyens* 2001 (4) SA 15 [SCA].
[25] *Smuts vs Booyens* para 17.
[26] *Smuts vs Booyens* para 17.
[27] *Inter se* is the Latin for "between the parties".

is therefore critical to establish what remedy the new shareholder has against the company, or the person from whom he bought the shares or the liquidator.

The focus of this research is on the plight of the person to whom shares were sold in a company which is being liquidated before transfer has taken place. Does the purchaser have any recourse against the transferor who had now made him the owner but not the shareholder of the shares or does he have an action against the company? Section 8(2)(b) of the Act provides that the transfer of shares of private companies must be restricted.[28] This means that in the case of private companies, restriction is mandatory.

Section 35(1) of the Act provides that shares issued by a company are moveable property and are transferable in any manner.[29] For the rest, the Act is silent on transfer, except maybe for section 51(6)(a) which provides that a company must enter the transfer of any certificated securities in its securities register.[30] This can only be done if the transfer is evidenced by a proper instrument of transfer that has been delivered to the company.[31] Section 51(1)(a)(iv) also suggests that restrictions can be placed on the transfer of shares.[32] It is therefore clear that the purchaser of shares will only become shareholder after transfer has been effected.

Cession alone does not make the purchaser a shareholder of the company and as a consequence ownership in the shares and shareholding in the company, remain split until registration. Only

[28] The Companies Act 71 of 2008, s 8(2)(b).
[29] Cassim, Cassim & Jooste 'et al' *The Law of Business Structures* (2015) 175.
[30] The Companies Act 71 of 2008, s 51(6).
[31] Cassim, Cassim & Jooste 'et al' *The Law of Business Structures* (2015) 175.
[32] The Companies Act 71 of 2008, s 51(1)(a)(iv); Cassim, Cassim & Jooste 'et al' *The Law of Business Structures* (2015) 175.

once the purchaser is registered as the shareholder will he be able to exercise the rights that are attached to the share.[33]

In the case of *Botha v Fick*[34] it was held that ownership in shares passes through cession. Cession is therefore only one of the elements of transfer.[35] The way a purchaser can ensure that the shares have been transferred to him in the proper way would be to adhere to the following:

Ensure that a written contract is in place, which clearly identifies that the seller wishes to sell, cede and transfer the shares in question to the purchaser. In addition to this ensure that the following documents have been delivered and are in the purchaser's possession.[36]

- "share transfer form signed by the exiting shareholder;
- the original share certificate pertaining to the shares;
- copy of the board resolution of the company; a certified extract of the share register reflecting that the purchaser is a shareholder in the company and the holder of the shares in question; and
    - consenting to the transfer;
    - undertaking to update the share register of the company; and
    - authorising two individuals to sign a new share certificate in your favour;
- a certified extract of the share register reflecting that the new owner is the shareholder in the company and the holder of the shares in question; and

[33] Cassim, Cassim & Jooste (2015) 175.
[34] *Botha v Fick* 1995 (2) SA 750 (AD)
[35] Vdma Corporate Commercial Attorneys 'Selling and Transferring Shares in to the Companies Act, 2008' available at *http://www.vdma.co.za/selling-transferring-shares-terms-companies-act-2008/* (accessed 4th August 2017).
[36] Vdma Corporate Commercial Attorneys 'Selling and Transferring Shares in to the Companies Act, 2008' available at *http://www.vdma.co.za/selling-transferring-shares-terms-companies-act-2008/* (accessed 4th August 2017).

- an original share certificate signed by at least two individuals authorised by the persons referred to in the board resolution."[37]

1.3 PURPOSE, OBJECTIVE AND SIGNIFICANCE OF THE STUDY

This study analyses the problems pertinent to the transfer of shares of a company that is being wound up, highlighted by *Smuts v Booyens* and by analysing the relevant sections of the Act, common law, case law and experiences from other jurisdictions it is the hope of the author that it will provide a solution to the problem or some form of recourse to the purchaser. The purpose is to:

1. Critically analyse the process of the transfer of shares during the liquidation of a company.
2. Draw from the experiences from other jurisdictions to improve the mode of transfer of shares during liquidation of a company.

By drawing from the experiences from other jurisdictions such as Australia and the United Kingdom it is the aim of the author that this study will contribute new knowledge and enrich Corporate and Insolvency law in South African.

1.4 RESEARCH METHODOLOGY

In light of the purpose of the study as an analytical study that draws on experiences from South Africa and other jurisdictions, a desktop methodology will be appropriate. The methodology

[37] Vdma Corporate Commercial Attorneys 'Selling and Transferring Shares in to the Companies Act, 2008' available at *http://www.vdma.co.za/selling-transferring-shares-terms-companies-act-2008/* (accessed 4th August 2017).

will involve an analysis of primary sources such as legislation and case law. The secondary sources of law will include journal articles, text books, thesis and internet sources. Borrowing from other jurisdictions is critical to improving the interpretation and understanding of South Africa law. The consideration of foreign and international law is encouraged in so far as it is consistent with the Constitution of the Republic of South Africa, 1996 (the constitution).[38] English company law principles have had a long standing relationship with South African company law.[39] As such reference to English company law principles will be used to better understand and interpret South African company law. The legal framework of the UK and Australia will add value to the interpretation of South African company law. In addition, the comparators of choice are common law jurisdictions just like South Africa and as such these comparators are well suited for this study.

1.5 LIMITATIONS OF THE STUDY

This study is a critical analysis of various sections in the Act as well as schedule 5 of the Act, comparable provisions and case law in other jurisdictions such as the United Kingdom and Australia. With regard to the Act, the study limits itself to sections 8(2)(b), 15(6) and schedule 5. Close analysis of the historical background to the transfer of shares is necessary as it will be difficult to understand the extent of the research problem without referring to its history. Very little has been written about this particular issue and the *Smuts v Booyens* case is still the leading authority on this particular matter.

[38] The Constitution (1996), s 39(1)(b) and (c).
[39] Government Gazette No. 26493 (Notice 1183 of 2004) 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform' 3.

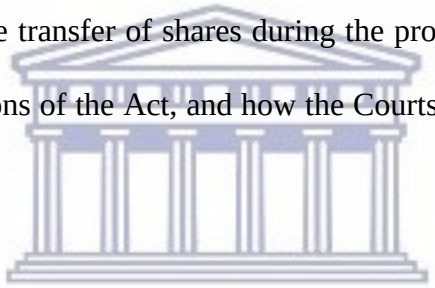
1.6 PROPOSED STRUCTURE

The study will be subdivided into five chapters as follows:

Chapter one will offer an introduction to the study, background, research arguments and the methodology of the study.

Chapter two will look at the transfer of shares in terms of the common law and legislation with specific emphasis on sections 8(2)(b), 15(6) and schedule 5 of the Act.

Chapter three will examine the transfer of shares during the process of liquidation. This will involve looking at the provisions of the Act, and how the Courts have interpreted them in the subsequent judgments.



Chapter four will examine the transfer of shares during the process of liquidation in the United Kingdom and Australia and developments made to deal with the transfer of shares during liquidation. This will be done by involving an analysis in light of SA's position

Chapter five will give conclusions, findings and recommendations to the study.

1.7 CONCLUSION

Company law provides the basis for one of the most important institutions organising and urging the South African economy, namely corporate business entities.[40] Corporations are

[40] Government Gazette No. 26493 (Notice 1183 of 2004) 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform' 5.

essential to the country's economy spurring its creation for wealth and comfort and social renewal.[41] While the decision to modernise South Africa's company law by the Department of Trade and Industry was aimed at bringing our law in line with international trends and mirror our ever- changing business environment, it did not adequately consider the transfer of shares during liquidation.[42] The researcher seeks to provide clarity in the area of transfer of securities and answering the research problem presented in a manner which reflects the principles and standard of South Africa's new corporate law reform.

[41] Government Gazette No. 26493 (Notice 1183 of 2004) 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform' 5.

[42] Government Gazette No. 26493 (Notice 1183 of 2004) 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform' 5.

CHAPTER TWO

THE TRANSFER OF SHARES IN TERMS OF THE COMMON LAW AND LEGISLATION WITH SPECIFIC EMPHASIS ON SECTION 20(1) OF THE 1973 COMPANIES ACT AND SECTION 8(2)(b) OF THE 2008 COMPANIES ACT

2.1 INTRODUCTION

The previous chapter offered a background, research problem, purpose and significance of the study. In addition, it offered the methodology, limitations and proposed structure to the study. This chapter analyses sections 8(2)(b) and schedule 5 of the 2008 Act as well as section 20(1) of the 1973 Act. The research problem raised in chapter one deals with the transfer of shares after the commencement of the process of winding-up. A purchaser's right to the shares is left to the discretionary decision made by the Liquidator. This is in terms of the transitional arrangements as set out in Schedule 5 of the Act, relating to the winding-up of insolvent companies, which provides that the now repealed Companies Act of 1973 remains in force in terms of Chapter XIV. Section 341(1) of the Old Act provides that such a transaction shall be void without the sanction of the Liquidator.[43]

When interpreting section 341(1) it would mean that where a private company's shares are sold and the company subsequently is wound-up on the grounds of insolvency before the shares are registered in the company's securities register in the name of the person who acquired the shares, transfer would be void in terms of section 341(1) unless sanctioned by the Liquidator.[44] The issue then focuses on the recourse of the purchaser in such an instance.

[43] The Companies Act 61 of 1973, s 341(1).
[44] The Companies Act 61 of 1973, s 341(1).

2.2 TRANSFERABILITY OF SHARES

A share is a personal right and is transferred by means of cession.[45] Shares are generally transferred in the manner provided for by the Act and the MOI of the company, and until the name of the transferee is registered in the company's securities register, the rights in the shares remain vested in the transferor.[46]

2.2.1 The Nature of a Share

According to Henochsberg on the Companies Act 71 of 2008, a share consists of a bundle of personal rights granting the holder thereof a certain interest in the company, its assets and dividends. Shares are incorporeal property and is considered to be movable property as it is transferable in any manner recognised by the Act.[47] In *Liquidators, Union Share Agency v Hatton*,[48] Innes CJ emphasised that, "A share in a joint stock company is a *jus in personam*, a right of action, the extent and nature of which and the liability attaching to the ownership of which depend upon statute."[49]

2.2.2 Transfer of proprietary rights in shares

A 'share' is the proprietary right that a person holds in a company.[50]

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45 *Liquidators, Union Share Agency v Hatton* 1927 AD 240.
46 Gibson JTR *South African Mercantile and Company Law* (2003) 310.
47 Schoeman-Louw N 'South African Company Law: what is your business a or share therein really worth available at *https://www.schoemanlaw.co.za/wp-content/uploads/2015/03/Value-of-shares-in-private-companies-MAR-2015.pdf* (accessed 17 September 2018).
48 *Liquidators, Union Share Agency v Hatton* 1927 AD 240.
49 1927 AD 240 at 250; *Smuts v Booyens* (2001) para 7.
50 Cassim FHI, Cassim MF, Cassim R 'et al' *The Law of Business Structures* (2015) 163.

In *McGregor's Trustees v Silberbauer,*[51] McGregor, sold his shares for which he received payment and delivered the certificates to the purchaser. He then surrendered his estate before the transfer was registered in the books of Colonial Marine Assurance Co. and Colonial Fire Assurance Co.[52] The trust deeds of both companies provided that the transfer of shares needed authorisation by the directors and until it was registered it would not have effect.[53] The directors of the two companies were ready and willing to register the shares in the name of the purchaser, Silberbauer, but the plaintiffs (the trustees of McGregor's insolvent estate), objected thereto and gave notice not to register the shares.[54]

The plaintiffs argued that it was evident from the trust deeds of the company that the shares remained the property of the insolvent estate, while Silberbauer argued that the shares were his property. The court held delivery is required. During the course of his decision CJ De Villiers referred to *Harris v Buissine*[55], where it was held that title was not complete until registration.[56] CJ De Villiers contended "that the principle laid down in *Harris v Buissine* ought to be extended to cases of sales of shares and the insolvency of the vendor before registration of the shares in the name of the purchaser has been effected.[57]

Although the court considered it bound to that decision the Chief Justice intimated that the court would do nothing to extend the rule to cases that do not clearly fall within the principle of the rule.[58] The question then becomes this: what right does the purchaser of shares obtain

[51] *McGregor's Trustees v Silberbauer* (1891) 9 SC 36.
[52] McGregor's Trustees v Silberbauer (1891) 9 SC at page 36.
[53] *McGregor's Trustees v Silberbauer* (1891) at page 37.
[54] *McGregor's Trustees v Silberbauer* (1891) at page 37.
[55] *Harris v Buissinee* (1840) (2 Menz, 105).
[56] *McGregor's Trustees v Silberbauer* (1891) at page 37.
[57] *McGregor's Trustees v Silberbauder* (1891) at page 38.
[58] *McGregor's Trustees v Silberbauder* (1891) at page 38.

against the insolvent estate where the seller has done everything in his power to transfer the shares?

The court held that in the case of the cession of a right the cession is complete when the cedent has done everything in his power to effect the transfer of his right.[59] In other words, ownership was conveyed by the effective and complete conveyance of the right of action represented by a share, which conveyance was accomplished by the transferor doing everything in his power to deprive himself of his interest. He did this by delivering his interest in the shares to the transferee by means of share certificates in negotiable form.[60]

The court also referred to the case of *Wright v The Colonial Government*[61] in which it was held that no particular form of words for the purpose of effecting a complete cession of action was required.[62] However, what is required is that the intention to effect the cession should be clear and beyond doubt and that no further act is necessary to complete the cession.[63] The court held that in this case, it is not a question of the title of a movable or an immovable but rather a question of the conveyance of a right of action.[64] Such a right is conveyed as soon as the transferor has done everything in his power to divest himself of his right of action. The court held, "that as the seller had done all in his power to complete the transaction, the shares belonged to the purchaser, and were not assets vested in the trustee of the seller's insolvent estate."[65]

[59] *McGregor's Trustees v Silberbauder* (1891) at page 38.
[60] *McGregor's Trustees v Silberbauder* (1891) at page 36.
[61] *Wright v The Colonial Government* 1891(8) SC 260; see also *Botha v Fick* 1995 (2) SA 750 A page 136.
[62] *McGregor's Trustees v Silberbauder* (1891) at page 38; *Wright v The Colonial Government* 1891(8) SC 260.
[63] *McGregor's Trustees v Silberbauder* (1891) at page 38; *Wright v The Colonial Government* 1891(8) SC 260.
[64] *McGregor's Trustees v Silberbauder* (1891) at page 39.
[65] *McGregor's Trustees v Silberbauder* (1891) at page 37.

In the case of *Botha v Fick*[66] the court referred to the principle as enunciated in *McGregor's v Trustees v Silberbauer* and accepted as good law that "a cession of shares is complete as between the parties when the cedent has done all in his power to divest himself of his right of action and to put the transferee in a position to demand recognition by the obligor…."[67] It was also held that cession does not have to be in writing, it can be tacit or inferred by the conduct of the parties.[68] The parties imply their intention by means of the signed share transfer form and by submitting it to the company.[69]

2.2.3 The contrast of ownership and registered title

South African company law recognises that there is a distinction between the registered holder of a share and the beneficial owner of a share.[70] In terms of section 140A of the 1973 Companies Act the registered holder is the person who appears in the share register of the company and who is the member of the company.[71] A beneficial owner, when used in relation to a company's securities, is a person who has the right or entitlement through ownership to exercise any or all rights attaching to the company's securities, to receive or participate in any distribution and dispose or direct the disposition of the company's securities.[72] In other words, 'beneficial owner' is a legal term where specific property rights in equity belong to a person even though legal title of the property belongs to another.

66 *Botha v Fick* 1995 (2) SA 750 at page 15.
67 1995 (2) SA 750 at page 15.
68 *Botha v Fick* 1995 (2) SA 750 (A).
69 du Plessis R 'Should different rules apply to the transfer of ownership in certificated and uncertificated securities available at *https://www.bowmanslaw.com/insights/finance/should-different-rules-apply-to-the-transfer-of-ownership-in-certificated-and-uncertificated-securities/* (accessed 18 June 2018).
70 du Plessis R 'Should different rules apply to the transfer of ownership in certificated and uncertificated securities available at *https://www.bowmanslaw.com/insights/finance/should-different-rules-apply-to-the-transfer-of-ownership-in-certificated-and-uncertificated-securities/* (accessed 18 June 2018).
71 The Companies Act 61 of 1973, s 140A.
72 The Companies Act 71 of 2008, s 1.

In terms of the 2008 Act a shareholder is defined as "the holder of a share issued by a company and who is entered as such in the certificated or uncertificated securities register."[73] Section 57(1) goes on to provide that a shareholder is the person "who is entitled to exercise any voting rights in relation to a company, irrespective of the form, title or nature of the securities to which those voting rights are attached."[74] The registered shareholder can enforce his rights as shareholder against the company.

The beneficial owner does not appear in the share register but is entitled to the benefits flowing from the share. This means that the beneficial owner or the holder of the beneficial interest in the share has no rights against the company and receives his benefit from the registered shareholder under an arrangement between the two of them.[75] At this point it is prudent to revert back to section 341 of the 1973 Act. If section 341 finds application and the liquidator through his discretion has declared the sale of the shares void, section 341 would imply that the buyer has no rights against the company and the only remedy would then lie against the seller.[76] It is therefore important to determine how the courts have dealt with this matter. It is important to note that *Smuts v Booyens* is an integral part of this process as the courts still view this case as leading authority when dealing with the transferability of shares in private companies.

[73] The Companies Act 71 of 2008, s 1.
[74] The Companies Act 71 of 2008, s 57(1).
[75] du Plessis R 'Should different rules apply to the transfer of ownership in certificated and uncertificated securities available at *https://www.bowmanslaw.com/insights/finance/should-different-rules-apply-to-the-transfer-of-ownership-in-certificated-and-uncertificated-securities/* (accessed 18 June 2018).
[76] The Companies Act 61 of 1973, s 341.

2.3 TRANSFER OF SHARES UNDER THE 1973 ACT

In the case of *Smuts v Booyens*[77] the primary question before the court was "whether a private company's shares may be transferred to an innocent third party in violation of provisions in the company's own articles of association."[78] The court held that in terms of the 1973 Act it was irrelevant that the purchaser was unaware of restrictions on the transfer of company shares.[79] The principal argument was that the provision in the company's articles amounted to an agreement not to transfer the rights, in other words, a *pactum de non cedendo*[80]. The trial court held that in the absence of compliance with the procedures in the articles it precluded the third party, Booyens, from ever becoming the owner of the shares.[81]

On appeal the primary question was whether the court a quo was correct in finding that proof was necessary that Booyens knew about the provisions in question and the non-compliance of such provisions. The court held that in previous analogous cases where a private company's articles were enforced, the purchaser's awareness of the prohibition was not in issue and the articles in any event contained an express prohibition on transfer.[82] "Counsel for Booyens rightly conceded that finding that Booyens' knowledge of the prohibition was irrelevant must lead to the appeal succeeding and that the other shareholder in the company, Smuts would be entitled to consonant relief."[83]

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77 *Smuts v Booyens, Markplaas (Edms) Bpk en 'n Ander v Booyens* (2001) 4 SA 15 (SCA).
78 *Smuts v Booyens* (2001) para 1.
79 Cassim (2012) 76.
80 *Pactum de non cedendo* meaning anti-cession or non-cession clause, in these terms meaning "You shall neither cede any of your rights nor assign any of your obligations under this agreement without our prior written consent." Meaning it is an n agreement not to cede. Hiemstra VG & Gonin HL *Trilingual Legal Dictionary* 3 ed (2012) 251.
81 *Smuts v Booyens* (2001) para 6.
82 See *Estate Milne v Donohoe Investments (Pty) Ltd and Others* 1967 (2) SA 359 (A) and *Lombard v Suid Afrikaanse Vroue-Federasie, Transvaal* 1968 (3) SA 473 (A). Compare also *Swart v Celliers* 1976 (2) PH E10 (K) (where the purchaser acquired knowledge of restrictions on transfer), *Mendonides v Mendonides and Others* 1962 (2) SA 190 (D) and *Britz N.O. v Sniegocki and Others* 1989 (4) SA 372 (D).
83 *Smuts v Booyens* (2001) para 6.

The court held that the starting point in answering this question must be the provisions of the 1973 Companies Act.

Under section 20(1) of the 1973 Companies Act the expression 'private company' means:

> "a company having a share capital and which by its articles—
>
> (a) restricts the right to transfer its shares; and
>
> (b) limits the number of its members (exclusive of persons who are in the employment of the company and of persons who having been formerly in the employment of the company were, while in such employment, and have continued after the termination of such employment to be, members of the company) to fifty; and
>
> (c) prohibits any offer to the public for the subscription of any shares or debentures of the company."[84]

These provisions raise the comment that transfer restrictions in respect of shares are an indispensable characteristic of a private company. By its very definition a private company contains this restriction in its Articles of Association (AOA), the absence of which it is legally impossible for an entity to be a private company.[85]

The provision shows that a private company's AOA must limit the transfer of its shares and thus accordingly restrict 'the right' to conclude the entire series of steps that embraces a

[84] Section 20(1) of the Companies Act 61 of 1973.
[85] *Smuts v Booyens* (2001) para 8.

transfer. This involves the conclusion of an agreement to transfer, the execution of a transfer deed and the registration of the transfer.[86]

"The opposing view is that a shareholder who fails to comply with a restriction on 'transfer' is not prohibited from transferring the beneficial ownership of shares (by way of cession, which requires no formalities), and the Act merely prohibits and denies the right to have the transfer registered."[87] The courts have not accepted this counterargument and the current position remains as in terms of common law as decided in *Smuts v Booyens*.[88]

In *Smuts v Booyens*[89] the court held that transfer restrictions in respect of shares in the context of section 20(1) of the 1973 Act is an essential characteristic of a private company.[90] By definition a private company is an entity that contains this restriction in its AOA and thus in the absence of this it is legally impossible for the entity to be a private company.[91] These restrictions speaks to the legal nature and essence of a private company. This means that if any restrictions on transferability in terms of the company's constitution are not adhered to then the shares are not transferable at all. A shareholder must comply with the procedure for transfer and the restrictions on transfer in a private company's constitution in order for a transfer of shares to be legal. Failing this no rights in respect of such shares may be transferred to the purchaser and the rights will lack transmissibility *ab inito*[92]. The restriction on transmissibility is absolute in the form of a *pactum de non cedendo*.[93]

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86 Section 20(1)(a) of the Companies Act 61 of 1973; *Smuts v Booyens* (2001) para 10.
87 Cassim (2012) 76.
88 Cassim (2012) 76; Larkin MP & Cassim FHI 'Company Law' (2001) Annul Survey of South African Law 547-8.
89 2001 (4) SA 15 [SCA].
90 Cassim FHI, Cassim MF, Cassim R 'et al' *Contemporary Company Law* (2012) 2ed 76; *Smuts v* Booyens (2001) para 8.
91 *Smuts v Booyens* (2001) para 8.
92 From inception / from the beginning. Hiemstra & Gonin (2012) 147.
93 *Pactum de non cedendo* meaning anti-cession or non-cession clause, in these terms meaning Agreement not to cede "You shall neither cede any of your rights nor assign any of your obligations under this agreement

The use of the words 'the right' in section 20(1)(a) is noteworthy as it refers to the fact that 'the right' to transfer must be restricted, as it points to the legislature's intention that the shareholders' capacity to transfer his shares has to be limited by the AOA.[94] It also means that a transfer "in the full and technical sense" embraces a series of steps that include the finalisation of an agreement to transfer.[95] In other words what the AOA must restrict is "the right" to conclude the whole series of steps that a transfer embraces.[96]

2.4 TRANSFER OF SHARES UNDER THE 2008 ACT

Under the 2008 Act it is still necessary for a private company to include a restriction with regard to the transferability of its shares in its MOI. However, the reference to 'shares' has been extended to a restriction on transferability of 'securities'. These securities include 'any shares, debentures or other instruments.[97] This restriction can be found under section 8(2)(b) of the 2008 Act thus meaning that in order for a company to qualify as a private company the company's MOI must in terms of section 8(2)(b) of the Act, limit the transferability of its securities.[98] These new transferability restrictions must be read within the context of the transitional provisions contained in schedule 5 of the Act.[99]

Section 8(2)(b) of the Act provides that a private company in terms of its MOI must prohibit the company from offering and restricting the transferability of its securities to the public.[100]

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without our prior written consent."; Hiemstra & Gonin (2012) 251; Cassim (2012) 76; *Smuts v Booyens* 2001 (4) SA 15 [SCA].

94 *Smuts v Booyens* (2001) para 9.

95 *Smuts v Booyens* (2001) para 10.

96 *Smuts v Booyens* (2001) para 10.

97 Gertsle L 'The transferability of securities - another drafting conundrum' (2013) 13 *Without Prejudice* 30.

98 Section 8(2)(b) of the Companies Act 71 of 2008; Gertsle (2013) 30.

99 Gertsle (2013) 30.

100 The Companies Act 71 of 2008, s 8(2)(b).

This means that in the case of private companies this restriction is obligatory.[101] Our courts are rather reluctant to restrict transferability[102] and generally, shareholders have the right to deal freely with their shares. However, in *Smuts v Booyens*, Cameron JA referred to *Estate Milne v Donohoe Investments (Pty) Ltd*[103] where it was pointed out that the restriction on transfer in the articles is "essentially one of construction of the relevant articles" and "the *prima facie*[104] right of a shareholder to deal freely with his shares must perforce yield to contrary provisions ascertained on a correct construction of the company's articles."[105]

Companies generally impose restrictions to allow existing shareholders a degree of control over the identity of the company's shareholders to either preserve an existing pattern of control or to preclude one or more shareholders from gaining control by purchase from other shareholders.[106] A common way of placing a restriction on transferability is by making the right to transfer subject to a right of pre-emption. This would mean that if a shareholder wishes to dispose of his shares in a company he must first offer the shares to the other shareholders in the company before the shares can be sold to a third party.

In the event a shareholder ignores a pre-emptive right and sells his shares, the sale to the purchaser is valid but the shareholder is prevented from ceding his rights to the purchaser in terms of such a sale. Thus the supposed cession of the rights to the purchaser is void.[107]

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[101] Hefer L 'Transferability of shares, pre-emptive rights and S39' available at *http://www.onlinemoi.co.za/how-transferable-are-private-company-shares* (accessed 01 March 2018).

[102] Hefer L 'Transferability of shares, pre-emptive rights and S39' available at *http://www.onlinemoi.co.za/how-transferable-are-private-company-shares* (accessed 01 March 2018); See also *Greenhalgh v Mallard, Delavenne v Broadhurst, Smith v Fawcett Ltd, Moodie v W&J Shepherd (Bookbinders) Ltd, Greenacre V Falkirk Iron Co Ltd, Estate Milne v Donohoe Investments (Pty) Ltd, Bellairs v Hodnett* and *Commercial Grain Producers Association v Tobacco Sales Ltd.*

[103] *Estate Milne v Donohoe Investments (Pty) Ltd* 1967 (2) SA 359 A at 370 F-G.

[104] *Prima facie* meaning; on the face of it. Hiemstra & Gonin (2012) 259.

[105] *Smuts v Booyens* (2001) para 16.

[106] Hefer L 'Transferability of shares, pre-emptive rights and S39' available at *http://www.onlinemoi.co.za/how-transferable-are-private-company-shares* (accessed 01 March 2018).

[107] Hefer L 'Transferability of shares, pre-emptive rights and S39' available at *http://www.onlinemoi.co.za/how-transferable-are-private-company-shares* (accessed 01 March 2018).

2.5 CONCLUSION

Currently the transferability of shares is restricted in the context of *Smuts v Booyens* case. If any restrictions on transferability in terms of the company's constitution are not adhered to then the shares are not transferable at all.[108] Shareholders must comply with the procedure for transfer of shares or the restrictions on transfer in order for a transfer to be legal. Failing this no rights in respect of the shares may be transferred to the purchaser and the rights thereto will lack transmissibility. The restriction on transmissibility is absolute in the form of a *pactum de non cedendo*.[109]

Legislation relating to the winding-up of insolvent companies continues to be regulated by the provisions of the 1973 Act and the transitional arrangements as set out in schedule 5 of the 2008 Act until such time it is replaced by other appropriate legislation. There is a wealth of developed case law concerning the winding-up of an insolvent company as well as cases relating to the transfer of securities during liquidation process.[110] The next chapter will examine the transfer of shares during the process of liquidation which will involve looking at provisions of the Act and how the Courts have interpreted them in subsequent judgments. The findings of the *Smuts v Booyens* is integral to this research therefore a further analysis of the case will be made in the next chapter.

[108] Cassim (2012) 76; *Smuts v Booyens; Markplaas (Edms) Bpk v Booyens* 2001 (4) SA 15 [SCA].

[109] *Pactum de non cedendo* meaning anti-cession or non-cession clause, in these terms meaning agreement not to cede. "You shall neither cede any of your rights nor assign any of your obligations under this agreement without our prior written consent." Hiemstra & Gonin (2012) 251; Cassim (2012) 76; *Smuts v Booyens* 2001 (4) SA 15 [SCA].

[110] Cassim (2012) 918.

CHAPTER 3

THE TRANSFER OF SHARES DURING THE PROCESS OF LIQUIDATION: A SOUTH AFRICAN APPROACH

3.1 INTRODUCTION

This chapter will examine the transfer of shares during the process of liquidation by looking at related provisions of the Act and how South African Courts have interpreted them in subsequent judgments. As mentioned in chapter one the concept of transfer of shares is interpreted as a series of steps. If the transfer is executed after the commencement of the winding-up process a purchaser's right to the shares are left to the discretionary decision of the liquidator.[111]

3.2 TRANSFERABILITY OF SECURITIES

Shares are generally freely transferable. However, the MOI or company rules may place restrictions on transferability. Courts are reluctant to restrict transferability and provisions that limit transfer are interpreted restrictively.[112]

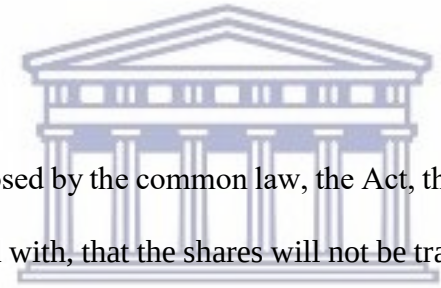
3.2.1 Restrictions on Transfer

As mentioned in chapter two, shareholders have the right to deal freely with their shares, but in terms of section 8(2) (b) of the Act a private company's MOI must restrict the transferability

[111] The Companies Act 61 of 1973, s 341(1); Schedule 5 of the Companies Act 71 of 2008.
[112] Hefer L 'How Transferable are Private Company Shares?' available *at* *http://www.onlinemoi.co.za/how-transferable-are-private-company-shares* (accessed on 12 October 2017).

of its securities.[113] A public company is undefined in the Act but is defined by exclusion in the sense that it is a company that is not a private company or any other type of profit, company.[114] Unlike a private company, the shareholders in a public company may freely offer securities to the public, unless the company elects to impose restrictions on the transferability of securities.[115] This means that public companies are given the option to import restrictions in the MOI or rules, but this does not happen often. There are many reasons for restriction but generally it would be to allow shareholders a measure of control over the identity of the company to either maintain an existing pattern of control, restricting speculation or preventing one or more shareholders from obtaining control by purchase from other shareholders.[116]

3.2.2 Effect of Restriction



The effect of restrictions imposed by the common law, the Act, the MOI, rules or shareholders' agreements is, if not complied with, that the shares will not be transferable at all. In the case of *Smuts v Booyens*[117] which is still the leading authority today, it was held that a transfer against a restriction is ineffective and void.[118]

The change of membership in the company's securities register happens by giving an instruction to the company to replace the existing shareholder with the new shareholder. This instruction is usually given by submitting a share transfer form. Ownership in the shares is transferred by way of cession of the rights in and to the shares. In *Botha v Fick*[119] it was said

113 The Companies Act 71 of 2008, s 8(2)(b).
114 Cassim FHI, Cassim MF, Cassim R 'et al' *The Law of Business Structures* 2015 83.
115 Cassim (2015) 83.
116 Cassim FHI, Cassim MF, Cassim R et al *Contemporary Company Law* (2012) 2ed 243.
117 *Smuts v Booyens; Markplaas (Edms) Bpk v Booyens* 2001 (4) SA 15 (SCA.
118 *Smuts v Booyens* (2001) para 3.
119 1995 (2) SA 750 (A).

that cession does not have to be writing, it can be tacitly given or it can be inferred by the conduct of the parties.[120]

A common restriction on transferability is making the transfer subject to a right of pre-emption.[121] In South Africa the term pre-emptive rights is a common form of restriction on the transfer of shares in private companies.[122] Such a provision will usually provide that a shareholder who wishes to sell his shares must first offer them to the other shareholders.[123] This provision will be made in the MOI and may read as follows:

> "A shareholder who wishes to dispose of his or her shares must first offer the shares to the other shareholders of the company pro rata to their existing shareholdings at a price to be determined in a prescribed way."[124]

The transfer in terms of the MOI includes the cession of the shareholder's right. Should a shareholder ignore a pre-emptive right and sell his shares to a third party, the sale to the purchaser would be valid. However, the rights in the shares are not transferred in terms of the sale.[125] It is not until the purchaser is registered in the securities register that he will attain the rights in the shares. Thus the purported cession of the rights in the shares to the purchaser is invalid.[126] This leaves the purchaser with an action for damages against the selling

120 Bowmans 'Should different rules apply to the transfer of ownership in certificated and un-certificated securities?' available at *http://www.bowmanslaw.com/insights/finance/should-different-rules-apply-to-the-transfer-of-ownership-in-certificated-and-uncertificated-securities/* (accessed 21 June 2018).

121 Pre-emption Right is a common form of restriction on transfer of shares in private companies; Cassim (2012) 244.

122 Van der Linde K 'Pre-emptive Rights in respect of share Issues – Misnomer or Mistake?' (2008) 20 *SA Merc LJ* 510; Delport P 'Pre-emption Rights and the Sale of Shares' (2003) 15 *SA Merc LJ* 264.

123 Cassim (2012) 244.

124 Hefer L 'How Transferable are Private Company Shares?' available *at http://www.onlinemoi.co.za/how-transferable-are-private-company-shares* (accessed on 12 October 2017).

125 Cassim (2012) 245.

126 Cassim (2012) 245.

shareholder.[127] The selling shareholder is still nevertheless bound to sell the shares to the other shareholders and if the other shareholders are not willing to take up the shares, then perhaps a right to claim cession of the balance of the shares.[128]

In the case of *Lyle & Scott Ltd v Scott's Trustees*[129] Lord Keith held that:

> "I think that a shareholder who has transferred, or pretended to transfer, the beneficial interest in a share to a purchaser for value is merely endeavouring by subterfuge to escape from the pre-emptory provisions of the article … A sale of a share is a sale of the beneficial rights that it confers, and to sell or purport to sell the beneficial rights without the title to the share is, in my opinion, a plain breach of the provision of [the article]."[130]

The MOI of a company may also give the directors the power to refuse to register a transfer without having to give reasons for their refusal.[131] In the case of *Re Smith & Fawcett Ltd*[132] the court held that:

> "the principles to be applied in cases where the articles of a company confer a discretion on directors with regard to the acceptance of transfer of shares are, for the present purposes, free from doubt. They must exercise their discretion *bona fide*[133]

127 Cassim (2012) 245.
128 Cassim (2012) 245.
129 [1959] AC763; [1959] 2 All ER 661 (HL).
130 *Lyle & Scott Ltd v Scott's Trustees* [1959] AC 763; [1959] 2 All ER 661 (HL); *Smuts v Booyens; Markplaas (Edms) Bpk v Booyens* 2001 (4) SA 15 (SCA); Cassim (2012) 244.
131 Cassim (2012) 245; Borrowdale A 'The Directors Power to Refuse Registration of Shares' (1985) 9 *SA Company LJ* 68.
132 *Re Smith & Fawcett Ltd* [1942] Ch 304; [1942] 1 All ER 542 (CA).
133 *Bona Fides* meaning good faith. Hiemstra & Gonin (2012) 161.

in what they consider – not what a court may consider – in the interests of the company, and not for any collateral purpose."[134]

In South Africa a common restriction found in the MOI of private companies is that the directors have unfettered discretion to refuse to register a transfer of any securities of the company without having to give reasons for such refusal.[135] This raises the concern to what extent does the board have discretion to refuse transfer and is such a clause still in line with the modern notions of public policy having regard to the fact that a shareholder's shares are his private property and may deal with the same freely. That said, section 15(6) of the Act provides that the MOI is an agreement between the company and the shareholders and if the MOI contains a restrictive condition then irrespective of the shareholder's freedom to deal with his shares he will still be bound by such restrictions.[136] Nonetheless, section 8(2)(b)(ii) provides that private companies must restrict the transfer of shares,[137], irrespective of the modern notions of public policy.

3.3 SOUTH AFRICAN CASE LAW RELATING TO THE TRANSFERABILITY OF COMPANY SHARES UNDER THE 2008 COMPANIES ACT

This issue arose in the case of *Visser Sitrus (Pty) Ltd v Goede Hoop Sitrus (Pty) Ltd.*[138]

The MOI of Goede Hoop Sitrus (GHS) contained the following clause:

134 Cassim (2012) 245; *Re Smith & Fawcett Ltd* [1942] Ch 304; [1942] 1 All ER 542 (CA).
135 Kleitman Y 'Board's power to refuse a transfer of shares: Visser Sitrus case' available at *https://financialmarketsjournal.co.za/boards-power-to-refuse-a-transfer-of-shares-visser-sitrus-case/* (accessed 21 June 2018).
136 The Companies Act 71 of 2008, s 15(6).
137 The Companies Act 71 of 2008) s 8(2)(b)(ii).
138 *Visser Sitrus (Pty) Ltd v Goede Goop Sitrus (Pty) Ltd and others* 2014 (5) SA 179 (WCC).

> "no shareholder may transfer the registered or beneficial ownership of any Ordinary Shares in the Company to any other party without first complying with the requirements for transfer as set out in the Act and in this MOI and obtaining the approval of the board for such transfer. The board may, at any time, decline to register any transfer of Ordinary Shares in the securities register of the Company without giving any reason therefor and the directors shall be deemed to have so declined until they have resolved to register the transfer."[139]

One of the shareholders of GHS, Visser Sitrus (VS) wished to sell his shares to a company that was in the process of consolidating control over GHS. The board of GHS was not happy with this situation and accordingly refused to transfer the shares without giving reasons for their decision. This decision was challenged by VS in court but did not succeed. The court held that this type of clause, namely that the board of GHS has discretion to refuse the registration of transfer and does not have to provide reasons for such refusal, is a common restriction on transfer of shares in the MOI of private companies.[140]

"Company legislation in South Africa, in keeping with Commonwealth corporate legislation, has always required a private company's constitution to restrict the transfer of the company's shares. This requirement has been retained in s8(2)(b)(ii) of the Companies Act (which, notably, refers to 'securities' and not 'shares' – securities includes shares but also a number of other instruments issued by profit companies such as debentures and bonds)."[141]

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139 *Visser Sitrus (Pty) Ltd v Goede Goop Sitrus (Pty) Ltd and others* 2014 (5) SA 179 (WCC) para 7.
140 *Visser Sitrus (Pty) Ltd v Goede Goop Sitrus (Pty) Ltd and others* (2014) para 7.
141 *Visser Sitrus (Pty) Ltd v Goede Goop Sitrus (Pty) Ltd and others* (2014) para 44.

The court held that to its knowledge the validity of such a clause has never been tested and counsel informed the court that they found no authority to that effect. The discretion of the board is exercised in what the directors *bona fide* consider to be the best interest of the company. This is simply inherent in nature of the fiduciary power of the board thus there is no general duty on the board of directors holding fiduciary powers to give reasons for their actions to those to whom their duties are owed. As it is, these duties are owed to the company and not to the shareholders. The court also mentioned that the standard power of directors has been dealt with by recent UK cases and confirmed its nature and validity.[142]

The 2008 Act, contains similar provisions under section 8(2)(b) as the 1973 Act under section 20(1), while section 15(6) of the Act deals with the relationship between shareholders *inter se*, shareholders and the company and directors and the company.[143] It is now accepted that the MOI constitutes an agreement between the company and the shareholders and between the shareholders themselves and between the directors and the company.[144]

It will be remembered that the focus of this research is on the plight of the person who became a shareholder in the company who is without remedy after the process of liquidation but before transfer has taken place. As he is now the owner of the shares in terms of cession but he is not written into the securities register of the company and as such not a shareholder. The question then becomes what recourse does the purchaser have.

One needs to consider who is making the disposition in a share transfer. It is clear that it is the shareholder making the disposition and not the company as the shares being transferred is

[142] *Visser Sitrus (Pty) Ltd v Goede Goop Sitrus (Pty) Ltd and others* (2014) para 45.
[143] The Companies Act 71 of 2008, s 15(6).
[144] The Companies Act 71 of 2008, s 15(6).

shareholder property and not company property.[145] This would mean that the new purchaser would have a right of action to claim damages from the shareholder and not the company in the event the company is in the process of winding-up after the shares has been ceded to the purchaser but before the purchaser is registered in the company's securities register as the new shareholder.

One also needs to consider that the original shareholder may have known that the company would be liquidated before the shares were sold to the purchaser. This may be difficult to prove but if it can be proven, then the purchaser ought to have a right to claim for damages against the shareholder and not the company with regard to the misleading and deceptive conduct by the shareholder. This has however, not been analysed in court and until such time that it is, *Smuts v Booyens* will continue to be the leading authority on this particular issue.

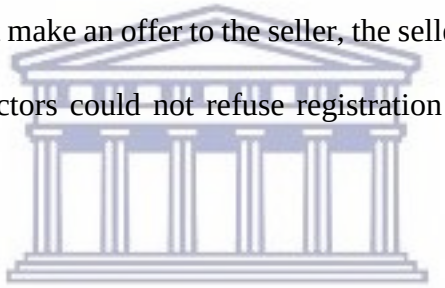
The relationship between shareholders under the 2008 Companies Act is the same now as it was at the time of *Smuts v Booyens* and the 1973 Act under section 341(1) and therefore the problem still remains.[146] Thus the plight of the purchaser who was made owner of the shares but not shareholder by the cedent will be exactly the same now in insolvency situations as it was then. There seems to be no remedy for a shareholder to whom shares have been transferred unless transfer took place before the winding-up process started.

[145] The Companies Act 61 of 1973, s 341.

[146] De Rebus The Law Reports 'Validation of Dispositions in terms of Section 341(2) of the Act' available at *http://www.saflii.org/za/journals/DEREBUS/2015/99.html* (accessed 21 January 2018).

3.4 SOUTH AFRICAN CASE LAW RELATING TO THE TRANSFERABILITY OF COMPANY SHARES UNDER THE 1973 COMPANIES ACT

In corporate law, the transfer of shares plays an important role and until *Smuts v Booyens*[147] courts were not always clear on the meaning of transfer. This case involved two shareholders, Smuts and Roux, who had a pre-emption right[148] in terms of articles 21 and 24 of the AOA of Markplaas.[149] The pre-emption right had the effect that if a member of the company wanted to sell his shares notification had to be made to the directors of this intention in writing. The price had to be stated as well as his willingness to accept the offer. Notice by the directors then had to be communicated to the remaining shareholders who could purchase the shares. If the remaining shareholders did not make an offer to the seller, the seller could then offer the shares to any other person. The directors could not refuse registration of the shares without good cause.[150]



Roux then transferred his shares to a third party, Booyens, without adhering to the pre-emption clause of the articles.[151] Subsequently Roux was sequestrated and after the sequestration order was granted, Roux delivered the share certificates to Booyens.[152] Booyens then brought an application for the rectification of the share register so that he may be reflected as the new shareholder. The court found that he was entitled to the shares on the basis of the sale and was entitled to be entered in the register as the new shareholder.[153]

147 *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 (4) SA 15 (SCA.

148 Pre-emption right is known in the context of private companies as a common form of restriction on the transfer of shares; Smuts v Booyens; Van der Linde K 'Pre-emption Rights in respect of Share Issues – Misnomer or mistake?' (2008) 20 *Merc LJ* 510.

149 Pretorius JT, Delport PA, Havenga M et al *Student Case Book on Business Entities* (2004) 167.

150 Delport P 'Pre-emption rights and the sale of shares' (2003) 15 *SA Merc LJ* 264.

151 Pretorius JT, Delport PA, Havenga M et al (2011) 167.

152 Delport (2003) 265.

153 Delport (2003) 265.

On appeal the matter was heard at the SCA against both orders.

Cameron JA accepted the definition of a share as given in *Liquidators, Union Share Agency v Hatton*[154] where it was said that 'A share in a joint stock company is a *jus in personam*[155], a right of action, the extent and nature of which and the liability attaching to the ownership of which depend upon statute.'[156]

The court discussed the importance of section 20(1)(a) which provides that a private company implies a company having a share capital and by its articles places a restriction on the transfer of shares in a private company.[157]

Cameron JA held that, firstly, transfer restrictions in respect of shares are 'indispensable characteristics of a private company' as it is defined in the Act.[158] This restriction is contained in the AOA of a private company and in its absence it is legally impossible for the company to be a private company. Secondly Cameron JA thought it significant that section 20(1)(a) required the 'right' to transfer shares to be restricted.[159]

"It points to the legislature's intention that the shareholders' capacity to transfer the private company's shares at all has to be limited by the articles of association."[160] Lastly, the Court reiterated that the word 'transfer' in the full and technical sense of the word included a series of steps as well as the conclusion of a transfer agreement.[161] This was explained in the *Inland*

154 1927 AD 240 at 250.
155 *Jus in personum* is a right of legal action against or to enforce a legal duty of a particular person or group of persons. A personal right arising from an obligation. Hiemstra & Gonin (2012) 215.
156 Delport (2003) 265; Pretorius JT, Delport PA, Havenga M (2004) 167.
157 The Companies Act 61 of 1973, s 20(1)(a); The equivalent to this section can be found under section 8(2)(b) of the Companies Act 71 of 2008.
158 *Smuts v Booyens* (2001) para 8.
159 *Smuts v Booyens* (2001) para 8; Delport (2003) 265.
160 *Smuts v Booyens* (2001) para 9.
161 *Smuts v Booysen* (2001) para 10.

Property Development Corporation (Pty) Ltd v Cilliers[162] (a case concerning section 24bix[163] of the Companies Act 46 of 1926):

> "In the regard to shares, the word 'transfer' in its full and technical sense, is not a single act but consists of a series of steps, namely an agreement to transfer, the execution of a deed of transfer and, finally, the registration of the transfer."[164]

According to Cameron JA, it was the intention of Parliament that 'transfer' be restricted in its full and technical sense and what the AOA must restrict is the 'right' to execute the entire series of steps that the transfer embraces.[165] That envelops the conclusion of an agreement to transfer, the execution of the deed of transfer and the subsequent registration of the transfer.[166] Cameron JA then stated that in view of section 20(1)(a) the restriction made it pre-emptory between the shareholders that the shares could not be transferred legally to a third party until the pre-emption procedure had been complied with.[167]

In *Borland's Trustee v Steel Brothers & Co Ltd* [168] the court held the restriction was an original characteristic of the share itself. This means that, "the right itself (the shares) could not be transferred if the pre-emption procedure had not been followed 'the right, from its inception, lacks the attribute of transmissibility."[169]

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162 1973 (3) SA 245 (A) at 251.

163 The shares of a private company may not be transferred to a third party in conflict with restrictions on the transfer contained in the company's articles of association as contained in articles 21-4 of Table B of Schedule 1 to the Companies Act 61 of 1973, even where the third party has no knowledge of those restrictions.

164 *Smuts v Booyens* (2001) para 10; Pretorius JT, Delport PA, Havenga M (2004) 168.

165 *Smuts v Booyens* (2001) para 10; Delport (2003) 265.

166 *Smuts v Booyens* (2001) para 10.

167 Delport (2003) 266.

168 *Borland's Trustee v Steel Brothers & Co Ltd* [1901] Ch 279.

169 Delport (2003) 266.

In *Smuts v Booyens* the court found that the procedure provided for in the AOA of Markplaas amounted to a *pactum de non cedendo*[170], in other words '[t]he stipulation against cession is part and parcel of the agreement creating the right, and the right is limited by the stipulation'.[171]

The judgment of the Supreme Court of Appeal (SCA) does not bode well for potential buyers of shares in private companies, as the failure to act in accordance by the seller with the pre-emption clause in the MOI or shareholders' agreement by the seller will have the effect that no rights in connection with the shares can be transferred to the buyer.[172]

This raises the question as to what is meant by 'rights in respect of shares'. Shares are rights, duties and obligations, and it is this combination that is transferred and not the rights in respect of these rights, duties and obligations.[173] Nonetheless, the purchaser, even if he has acted *bona fide*,[174] is in a hopeless position, as he cannot determine whether the pre-emption right has been complied with and can therefore only rely on the affirmation of the seller.

In *Smuts v Booyens* Cameron JA made the following comment: "South African case law refers repeatedly with approval to the judgment of Farwell J.[175] In my opinion this correctly portrays the interaction between the statutory basis on the one hand and the mutual contractual arrangement on the other that the articles of association of a company constitute."[176]

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170 *Pactum de non cedendo* meaning anti-cession or non-cession clause, in these terms meaning agreement not to cede. "You shall neither cede any of your rights nor assign any of your obligations under this agreement without our prior written consent." Hiemstra & Gonin (2015) 251.

171 at 25B, with reference to *Piages v Van Ryn Gold Mines Estate Ltd* 1920 AD 600; *Trust Bank of Africa Ltd v Standard Bank of South Africa Ltd* 1968 (3) SA 166 (A)); Delport (2003) 266.

172 Delport (2003) 266.

173 Delport (2003) 266.

174 *Bona Fide* meaning Good faith. Hiemstra & Gonin (2012) 161.

175 *Inter alia* by Innes CJ in *Liquidators, Union Share Agency v Hatton* 1927 AD 240 at 251.

176 *Smuts v Booyens* (2001) para 14.

The relevant provisions of Markplaas' AOA were analysed against this background. Articles 21-4 provided as follows:

> Article 21: "If a member of a company desires to sell all or any of his shares of the company he shall give notice, in writing, of his intention to sell, to the directors of the company, and state the price he requires for the shares.
>
> Article 22: The directors shall within one month of the date of receipt of the notice referred to in article 21 advise every other member of the company of the contents thereof and each such member shall be entitled to acquire the shares to be offered within one month after the date of the receipt of such advice: provided that if more than one member makes an offer for all the shares so offered, the shares shall be sold to each such member in equal proportions, and where fractional proportions of shares remain, such members shall become joint holders of such fractional proportions of the shares.
>
> Article 23: If the members of the company are unable to agree upon the selling price of the shares, the auditor of the company may be requested to determine the true and fair value thereof and the members shall accept that the value as the selling price of the shares.
>
> Article 24: If none of the members of the company offers to purchase the shares within the time referred to in article 22, or if member who is offering the shares for sale may offer the shares or the remaining portion of the shares which have

not been purchased by members of the company, for sale to any other person and, notwithstanding the provisions of article 11, the directors shall approve the registration of the shares in the name of that person unless they have good reason to refuse such registration."[177]

These are relevant aspects contained in the AOA of Markplaas and as such special attention can be drawn to three of these provisions namely articles 21, 22 and 24.

In terms of article 21 it is required of a shareholder who wishes to sell his shareholding to first give notice of his intention to the directors. Article 22 gives the other members 'the right' 'to acquire' the shares for sale before the shares in question may be offered to anyone else. The comparison between the provisions in the Act itself and article 22 of the AOA according to Thompson JA "is not merely coincidental: the "right" that according to section 20(1)(a) of the Act must be restricted is precisely the "right" that article 22 of the articles of association affords the other members".[178] This means to 'acquire' transfer of the shares by offer and acceptance and the completion of an agreement of sale. This is then followed by the execution of a deed of transfer and consequently followed by registration. Once these formalities have been complied with only then, does article 24 of the AOA grant the member the authority to offer the shares to an outsider for sale.

[177] *Smuts v Booyens* (2001) para 15; In *Estate Milne v Donohoe Investments*1967 (2) SA 359 (A) at 370F-G, Thompson JA specified that the restrictions in the AOA of a private company are "essentially one of construction of the relevant articles" and that "the prima facie right of a shareholder to deal freely with his shares must perforce yield to contrary provisions ascertained on a correct construction of the company's articles".

[178] *Smuts v Booyens* (2001) para 16.

This means that read in light of section 20(1)(a) of the Old Act, it would seem that the AOA of Markplaas encompass a mutual agreement between the shareholders of the company *inter se*[179] which in accordance with the statutory provision, impedes the right to transfer the company's shares by essentially requiring that the procedure as set out must in the first instance be followed before the shares can lawfully be transferred to an outsider. This further concludes that the restriction in the words of Farwell J, "constitutes an original incident of the shares themselves and that in the absence of compliance with the procedure the articles specify, no rights in the shares in question can be transfer to a purchaser".[180]

The mutual agreement in the AOA, in observance with the compulsory prescription of section 20(1)(a) of the Old Act contains a prohibition on the offer or transfer of the shares unless the procedure set out is first complied with. As such, if the preconditions are not complied with "the right, from its inception, lacks the attribute of transmissibility".[181] This means that the statutory provision restricts the right to transfer the company's shares by requiring the transfer procedure to be strictly followed before the shares can be lawfully transferred to a third party.[182] Thus is in the absence of compliance with the procedure the AOA specify, no rights in the shares can be transferred to the purchaser. Therefore, in order for the cessionary to gain the rights and become shareholder the other steps of 'transfer' must be adhered to, namely, registration in the company's share register.[183]

[179] Covenants entered into by all the shareholders inter se meaning between or among themselves.
[180] Refer to *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 (4) SA 15 (SCA) footnote 11 page 11 "Prof M S Blackman in Joubert, Lawsa (First Reissue) vol 4 part 1 para 232".
[181] Refer to *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 (4) SA 15 (SCA) footnote 12 page 11 "Cession", Joubert, Lawsa (First Reissue) vol 2 para 254. This is comparable to the case where contracting parties mutually agree that a specified right may be ceded only in accordance with a procedure that they prescribe: compare op cit para 246.
[182] *Smuts v Booyens* (2001) para 17.
[183] *Smuts v Booyens* (2001) para 17

The court held that Booyens' argument that the Act does not contain an absolute prohibition, but rather procedural rights that can be enforced by means of an interdict, was without foundation.[184] Instead the court held in favour of Smuts' argument that the AOA by implication create a *pactum de non cedendo* that prohibits transfer.

> "the stipulation against cession is part and parcel of the agreement creating the right, and the right is limited by the stipulation."[185]

The nature of a share was more comprehensively defined in *Standard Bank of SA Ltd v Ocean Commodities Inc*[186] by Corbett JA as:

> 'A share in a company consists of a bundle of conglomerate of personal rights entitling the holder thereof to a certain interest in the company, its assets and dividends.' "These are the rights to which a shareholder is entitled, and that actually comprise a 'share'".[187]

In the case of *Tigon Ltd v Bestyet Investments (Pty) Ltd*[188] the court highlighted the contrast:

> 'It seems to me that a distinction (not always recognised) may be drawn between the share itself, which is an incorporeal moveable entity, and the bundle of personal rights to which it gives rise … The incorporeals consisting of the

184 *Smuts v Booyens* (2001) para 18.
185 *Smuts v Booyens* (2001) para 18.
186 1983 (1) SA 276 (A) at 288.
187 Delport (2003) 268.
188 2001 (4) SA 634 (N) at 642±643.

shares, are, by statute, moveable property and possession is exercised by the holder negotiating, pledging, bequeathing or otherwise dealing in the shares.'[189]

The rights that comprise a share are also the same rights that a shareholder has against the company which are as distinct from the personal rights that the shareholder has as member as against other members.[190] This test can refine the issue: if there is a proposal that the right should be amended or terminated, the question is, does it require prior approval of the shareholders? If the answer to this question is yes, it is clear that this is a right that the shareholder has in his capacity as shareholder that is part of his personal rights that is a share and not a personal right in his capacity as member.[191] "Articles 21 and 24 of Markplaas restricted the rights of members to deal with their shares. As such it was their rights in their capacity as members that were restricted, not an 'original incident' of their shares".[192]

3.5 THE EFFECT OF LIQUIDATION ON SHAREHOLDERS

Two distinct and separate pieces of legislation regulate the winding-up of companies. The winding up of solvent companies is regulated in terms of sections 79 to 81 of Part G of Chapter 2 of the Act and the winding up of insolvent companies is regulated in terms of Chapter XIV of the Old Act.[193] This legislative divide is created by section 79(1)(b) of the Act as read with item 9 of Schedule 5 which prescribes the transitional arrangements of the Act. Item 9 of Schedule 5 provides "despite the repeal of the previous Act, until the date determined in terms of subitem (4), Chapter 14 of that Act continues to apply with respect to the winding-up and

189 2001 (4) SA 634 (N) at 642±643; Delport (2003) 268.
190 Delport (2003) 269.
191 *Cumbrian Newspapers Group Ltd v Cumberland and Westmoreland Herald Newspaper and Printing Co Ltd* [1986] 2 All ER 816; Delport (2003) 269.
192 Delport (2003) 269.
193 Cassim (2012) 918.

liquidation of companies under this Act, as if that Act had not been repealed subject to subitems (2) and (3)."[194]

If the company which is wound-up is solvent, the question then becomes what would happen in this instance and would it change anything? The liquidation is voluntary, in other words, the company is being dissolved but not because of insolvency. This would mean that the purchaser can be registered in the company's securities register and will attain the rights to the shares in the company. As a shareholder he would rank with the other shareholders and will be able to claim his money back from the estate of the company. On the other hand, if the liquidator does not give effect to the transfer then it means that the purchaser may have a claim for damages from the selling shareholder. However, this could be a costly process.

One also needs to ask what would happen if the liquidator decides to give effect to the transfer of shares of a company being wound-up due to its insolvency. First, the transfer would be complete and the effect of the transfer would make the purchaser a shareholder in the company. This would not be in the best interest of the purchaser to be a shareholder in a company where he paid for the shares that are now worthless because he would not rank with the creditors in the company.

He would only rank once all the creditors have been paid and if there is any money remaining in the company account. In a situation such as this it would be better not to have the liquidator give effect to the transfer so that the purchaser can have a claim for damages against the selling shareholder. Even though the purchaser will be the owner of the shares, if his name is not written in the securities register, he will not rank with the other shareholders. This does not

[194] Item 9 of Schedule 5 of the Act.

help the purchaser as the idea of the transaction is for the purchaser to become a shareholder in the stead of the selling shareholder and if this does not happen then surely the purchaser has a right to claim damages from the selling shareholder. These are the issues raised when considering the plight of the purchaser to whom the shares are either transferred or not transferred depending on the discretion of the liquidator and the position he is placed in if the liquidator decides not to give effect to the transfer.

The primary aim of an appointed liquidator is to close a company down and sell its assets whilst raising enough cash to pay off as many company debts as possible.[195] Whether it is compulsory or voluntary liquidation matters not, the result will be the same irrespective of the steps taken to get there. In a winding-up process of an insolvent company the creditors are placed first and thereafter shareholders are placed next in order of precedence. It is for this reason that shareholders rarely receive a dividend in an insolvent liquidation process unless they also have a creditor claim.[196]

[195] Clarke Bell 'How does liquidation affect shareholders' available at *https://www.clarkebell.com/blog/how-does-liquidation-affect-shareholders/ (*accessed 12 January 2018).

[196] Clarke Bell 'How does liquidation affect shareholders' available at *https://www.clarkebell.com/blog/how-does-liquidation-affect-shareholders/ (*accessed 12 January 2018).

3.6 CONCLUSION

Shareholders have the right to deal freely with their shares, and in terms of section 8(2)(b) of the Act a private company's MOI must restrict the transferability of its securities.[197] The transfer of shares is interpreted as a series of steps in a process that involves the execution of an agreement which can be contested under the law of contract. If the transfer is executed after the commencement of the winding-up process a purchaser's right to the shares are left to the discretionary decision by the Liquidator in terms of section 341(1) of the Old Act.[198]

The restriction of the transfer of shares in private companies is imposed by the common law, the Act, the MOI, rules or shareholders' agreements and the effect of non-compliance is that the shares will not be transferable at all. In *Smuts v Booyens* it was held that a transfer against a restriction is ineffective and void.[199] Cession alone does not make the purchaser a shareholder of the company and as a consequence ownership in the shares and shareholding in the company, remain split until registration. Only once the purchaser is registered as the shareholder will he be able to exercise the rights that are attached to the share.[200]

Smuts v Booyens is still the leading authority in this matter as the law has not changed in terms of the 2008 Act. Thus the relationship between shareholders is exactly the same now as it was at the time of *Smuts v Booyens* and the 1973 Act. As such there seems to be no remedy for a shareholder who has received shares in a company unless the transfer of such shares took place before the winding-up process commenced. There seems to be not much written about this particular issue in terms of various South African court judgments, thus in the next chapter the

197 The Companies Act 71 of 2008, s 8(2)(b).
198 The Companies Act 61 of 1973, s 341(1).
199 *Smuts v Booyens* (2001) para 3.
200 Cassim, Cassim & Jooste (2015) 175.

writer will look at the experiences of other jurisdictions in order to provide clarity in this regard and hopefully provide insight and contribute towards the interpretation of company law on this issue.

CHAPTER FOUR

THE TRANSFER OF SHARES DURING THE PROCESS OF LIQUIDATION: AN ANALYSIS OF THE EXPERIENCES IN AUSTRALIA AND UNITED KINGDOM

4.1 INTRODUCTION

Under South African law the concept of transfer of shares is interpreted as a series of steps in a process. As mentioned in chapter one, if the transfer is executed after the commencement of the process of winding-up, a purchaser's right to the shares is left to the discretionary decision made by the Liquidator.[201] In chapter three I analysed the transfer of shares during the process of liquidation by looking at related provisions of the South African Companies Act and how South African Courts have interpreted them in subsequent judgments.

Since very little has been written about this particular issue, this chapter will explore the experiences of other jurisdictions and investigate whether these experiences may be used to improve the mode of transfer of shares during liquidation of a company in South Africa. An analysis will be made of the jurisdictions of Australia and the United Kingdom in light of the position in South Africa.

The comparators of choice are common law jurisdictions just like South Africa with similar regimes on this specific topic and thus well suited for this study. Borrowing from these jurisdictions is critical to improving the law with regard to this particular issue.

[201] The Companies Act 61 of 1973, s 341(1) of and the transitional arrangements under Chapter 14 of the Companies Act 71 of 2008.

4.2 THE AUSTRALIA EXPERIENCE

Historically Australian Corporations law has borrowed heavily from company law in the United Kingdom. The legal structure of Australian Corporations law now consists of a single, national statute, the Corporations Act,[202] which is administered by a sole national regulatory Act authority, the Australian Securities and Investments Commission (ASIC). The Corporations Act under Chapter 5 section 468 governs the winding-up of companies.[203] The winding-up of a company in Australia takes the form of external administration under which a Liquidator assumes control of a company's affairs with the aim of discharging its liabilities in preparation for its dissolution.[204]

Once a company has been dissolved the ASIC will strike the company name off its register. If a company is in financial difficulty it can be put under the control of an independent external administrator whose role will depend on the type of external administration.[205] There are two types of winding-up processes namely court ordered winding-up also known as compulsory winding-up and voluntary winding-up which may be a member's winding-up or a creditor's winding-up.[206]

[202] The Corporations Act 50 of 2001.
[203] 'Winding up' available at *Sydney.edu.au/lec/subjects/insolvency/Winding%2Oup.doc* (accessed 23 April 2018).
[204] 'Winding up' available at *Sydney.edu.au/lec/subjects/insolvency/Winding%2Oup.doc* (accessed 23 April 2018).
[205] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).
[206] 'Winding up' available at *Sydney.edu.au/lec/subjects/insolvency/Winding%2Oup.doc* (accessed 23 April 2018).

4.2.1 Transfer of shares and restrictions on transferability

There are two main types of companies in Australia, proprietary companies (private) and public companies, the most common of which is proprietary companies.[207] A proprietary company is a personal liability company and the constitution of many proprietary companies contain pre-emptive rights that require shareholders to transfer shares to other shareholders first before those shares can be offered to third parties. By means of the company constitution the directors are given the right to refuse to register a share transfer without having to give reasons for their refusal to register.[208] In public companies pre-emptive right provisions are less common. Shareholders' agreements may however also provide restrictions on the transfer of shares although these restrictions are typically expressed to take precedence over restrictions in the company's constitution.[209]

4.2.2 Transfers in contravention of pre-emptive rights

When a pre-emptive rights provision has been breached, the question becomes, will a transfer of shares to a purchaser be invalid? .[210] In the case of *Rathner v Lindholm & Ors*,[211] the answer is 'not necessarily'. Whelan J found that the assignment of shares in Australian Enterprises Pty Ltd (AEPL) by the mortgagee of a company by the name of Advanced Communications Technologies Australia (ACTA) to the administrator of ACTA was in breach of AEPL's pre-

[207] DLA Piper 'Guide to going global – Corporate Australia' available at *https://www.dlapiperintelligence.com/goingglobal/* (accessed 10 October 2018).
[208] DLA Piper 'Guide to going global – Corporate Australia' available at *https://www.dlapiperintelligence.com/goingglobal/* (accessed 10 October 2018).
[209] DLA Piper 'Guide to going global – Corporate Australia' available at *https://www.dlapiperintelligence.com/goingglobal/* (accessed 10 October 2018).
[210] Windybank A & Ansell S SWS Lawyers 'Shareholders' pre-emptive rights – potential pitfalls' available at *https://www.swslawyers.com.au/news/shareholders-pre-emptive-rights-potential-pitfalls* (accessed 11 October 2018).
[211] [2005] VSC 399.

emptive rights regime. This pre-emptive rights regime applied to sales, transfer and assignment of AEPL's shares.[212]

This case dealt with the transfer of shares in breach of a pre-emptive rights provision of the company constitution of AEPL. ACTP owned 57.5 percent of the share capital in AEPL.[213] AEPL's constitution provided the following provisions:

> "A member may transfer all or any of his shares by an instrument in writing; the transferor remains the holder of the shares until the transfer is registered and the name of the transferee is entered in the register of members: paragraph 22.
>
> An instrument of transfer, accompanied by the certificate of the shares and such other evidence as the directors may reasonably require, is to be left for registration at the registered office of the company: paragraph 23.
>
> The directors have a wide power to refuse registration of a transfer in the following terms:
>
> The directors may (except where the transfer is to a member or person selected by them) refuse to register a transfer of shares without assigning any reasons for the refusal: paragraph 24(2).

[212] Windybank A & Ansell S SWS Lawyers 'Shareholders' pre-emptive rights – potential pitfalls' available at *https://www.swslawyers.com.au/news/shareholders-pre-emptive-rights-potential-pitfalls* (accessed 11 October 2018).

[213] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 29.

A member may not transfer a share unless rights of pre-emption in favour of other members, in accordance with a specified procedure, have been exhausted: paragraph 25."[214]

The shareholders' agreement also contained a relevant provision which provides as follows; "The shareholders' agreement is to prevail over the constitution if there is any inconsistency: clause 2.1.1."[215]

ACTA allowed a debenture charge over all its assets to Global Communications Technologies Pty Ltd (Global), including its shares in AEPL. Global appointed Mr Rathner (the Plaintiff) as the administrator of ACTA when ACTA was placed under administration. In accordance with a Deed of Settlement dated 17 August 2004, the Plaintiff, Global and its directors agreed that Global, as mortgagee in possession of the shares, would allocate the shares to the Plaintiff. Subsequently the Plaintiff tried to have the share transfer registered but the directors of AEPL refused to register the transfer, and accordingly the transfer was never registered.[216]

The defendants in the matter, namely, Mr Lindholm and Mr George (the first two defendants of nine), were appointed by Global, as receivers and managers of ACTA and who entered into an agreement with the other defendants to the proceedings, including the other shareholders of AEPL.[217] The plaintiff argued that the Defendants were not entitled to deal with the shares as the interest in the shares were transferred to the plaintiff as a consequence of the Deed of Settlement. The defendants argued that the Deed of Settlement did not grant the interest in the

[214] *Rathner v Lindholm and Others* [2005] VSC 399 para 7.
[215] *Rathner v Lindholm and Others* [2005] VSC 399 para 8.
[216] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 29.
[217] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 29.

shares on the plaintiff as the transfer was in breach of the pre-emptive rights provisions in the constitution.

The plaintiff also argued that there was no assignment of the shares that would violate the pre-emptive rights provisions contained in the constitution of AEPL and the shareholders' agreement as all that happened was that control of the shares changed from Global (ACTA's mortgagee) to the plaintiff in their capacity as the deed administrator of ACTA. The court held that clearly there had been assignment of the shares to the plaintiff, as the Deed of Settlement contained a clause concerning the transfer of shares, headed 'Assignment of AEPL Shares' which specified that Global was to 'assign' the shares to the plaintiff, acknowledge the plaintiff as the 'owner' of the shares and provided that Global was to execute and forward a share transfer form to the plaintiff in the plaintiffs favour.[218] It was held that the plaintiff had an equitable proprietary interest in the shares as a consequence of the assignment resulting from the Settlement Deed.

The issue then was, did the assignment contravene the pre-emptive rights of the other shareholders of AEPL and what the effect of such a contravention would be? The defendant maintained that any assignment or transfer in contravention of the constitution was entirely void. The court however noted that the trend in modern authorities was contrary to this approach.[219] Whelan J, engaged in an analysis of case law dealing with the issue of whether a transfer in contravention of pre-emptive rights is ineffective to transfer the interest in the shares to the transferee.

[218] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 29.
[219] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.

The judge confirmed that historically the courts have held that a transfer in contravention of pre-emptive rights is ineffective and unenforceable, as in *Hunter v Hunter*.[220] The court referred to relevant case law which strongly suggests that this is not the approach that the courts will take.[221]

In the case of *Hawks v McArthur*,[222] the shareholder, Mr McArthur, sold his shares to the purchasers, Messrs Fraser and Roberts, in contravention of pre-emption provisions. Mr Hawks was a judgment creditor of Mr McArthur and sought to execute on the shares still registered in Mr McArthur's name. Even though Messrs Fraser and Roberts paid the full purchase price, due to the contravention of the pre-emptive provisions the transfer was never registered.[223] Vaisey J held that the purchasers held the equitable interest in the shares and said the following:

"On general principles, in such circumstances as those of the present case where a man who has an interest in shares in a company received something for the sale of those shares and executes under seal a transfer of those shares for that purpose, I cannot bring myself to suppose that *Hunter v Hunter* constrains me to hold that everything done in that transaction is a complete nullity."[224]

In other words, the purchasers held an equitable interest in the shares and thus the transaction was not a 'complete nullity' and would prevail over a competing equitable interest which was second in time.[225] This is consistent with decisions that have broadly followed the decision in

[220] *Hunter v Hunter* [1936] AC 222.
[221] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.
[222] *Hawks v McArthur* [1951] 1 All ER 22.
[223] [2005] VSC 399 para 80; *Hawks v McArthur* [1951] 1 All ER 22.
[224] [1951) 1 All ER 27.
[225] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.

Hawks, where the Court held that "the competing interests to be determined were not between the purchaser and the shareholders, but rather between the purchaser and parties with a competing equitable interest."[226]

In terms of Australian law 'equitable interest' or 'equity interest' provides personal remedies such as specific performance.[227] The primary function of equity interest is to enforce personal rights, such as performance of a contract. Over time equity proved to award personal relief not only against owners of property but also against third parties who received such property.[228] This equitable personal relief was eventually perceived as having created a proprietary interest in favour of the party entitled to relief. This happened so routinely that ultimately a purchaser was treated in equity as if he held a property interest in the property once the contract was signed. "All equitable property rights are sourced in a personal obligation enforced in equity."[229]

With further reference to *Rathner v Lindholm,* Whelan J, also noted that a seller, who attempts to transfer his shares in breach of pre-emption provisions cannot count on this breach to evade the contract, however a purchaser is not so prohibited and may avoid the contract on this basis.[230] Although the purchaser may have an equitable right in the shares, the company and other shareholders of the company would not be bound by the share transfer by the selling

[226] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30; *Coachcraft Ltd v SVP Fruit Co Ltd & Champman* [1978] VR 706, *Tett v Phoenix Property & Investment Co.* [1984] BCLC 599, *Belmont Holdings Ltd v Permanent Trustee Co Ltd* [1989] 7 ACLC 420, *Hunters Beach Investments Pty Ltd v Bramms* (2001) ACSR 701, *Hurst v Crampton Bros (Coopers) Ltd* [2003] 1 BCLC 304, all these cases have broadly followed and accepted the approach in *Hawks v McArthur*.

[227] Bryan M & Vann V Equitable Proprietary Interests. In Equity and Trusts in Australia (2012) Cambridge University Press pp. 122 – 129.

[228] Bryan M & Vann V Equitable Proprietary Interests. In Equity and Trusts in Australia (2012) Cambridge University Press pp. 122 – 129.

[229] Bryan M & Vann V Equitable Proprietary Interests. In Equity and Trusts in Australia (2012) Cambridge University Press pp. 122 – 129.

[230] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.

shareholder in breach of the pre-emption provisions and the directors would have the power to deny registration of the transfer.[231] In the event the transfer is registered the shareholders may request that the registration by reversed. "An equitable interest held by a purchaser will not prevail over an interest held by a valid shareholder."[232]

In summary, the court held that even though legal title to the shares was not transferred to the Plaintiff, ACTA, due to the breach of AEPL's pre-emptive rights provision, ACTA had an equitable proprietary interest in the shares. Whelan J, held that, a purchaser's equitable proprietary rights will bind the seller of the shares, but in instances where a conflict exists between the rights of the purchaser and the rights of the shareholders other than the seller, the equitable rights of the other shareholders will succeed. In such a case, the seller would hold legal title to the shares on trust for the purchaser for its benefit or it subsequently complies with the pre-emption provisions and sells the shares to another party, it will hold the proceeds of sale on trust for the purchaser.

4.2.3 Post Liquidation Dispositions and Share Transfers

Under Australian Law the Liquidator's primary duty is to all the company's creditors. The shareholders rank behind the creditors and are unlikely to receive any dividend in an insolvent liquidation unless the shareholder also has a claim as a creditor.[233] In a court-ordered liquidation, the Liquidator is under no obligation to provide feedback to the shareholders on

[231] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.
[232] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 31.
[233] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

the progress or outcome of the liquidation. It is however, expected that the Liquidator keep records / books about the administration which gives a complete and correct record of the administration of the company's affairs and which records / books the shareholders are entitled to inspect at the Liquidator's office.[234]

Section 468A of the Corporations Act regulates the transfer of shares in a company that is made after the commencement of a winding-up by the court:

> "Section 468A Transfer of shares (1) A transfer of shares in a company that is made after the commencement of the winding-up by the Court is void except if:
>
> (a) Both:
>
> (i) the liquidator gives written consent to the transfer; and
>
> (ii) that consent is unconditional; or
>
> (b) all of the following subparagraphs apply:
>
> (i) the liquidator gives written consent to the transfer;
>
> (ii) that consent is subject to one or more specified conditions;
>
> (iii) those conditions have been satisfied; or
>
> (c) the Court makes an order under subsection (4) authorising the transfer."[235]

Section 468(1) of the Corporations Act provides that any disposition of the company, other than an exempt disposition, and any transfer of shares or alteration in the status of the members of the company made after the commencement of the winding-up by the court is, unless the

[234] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

[235] The Corporations Act 50 of 2001, s 468A.

court otherwise orders, void.[236] It is established that 'void' means void and not voidable. There are statutory exemptions under section 468(2). These exemptions include dispositions by the Liquidator, dispositions by an administrator and dispositions under a deed of the company arrangements which have been executed by the company and certain payments by Australian banks. These are *bona fide*[237] payments out of the company's account and in the course of the bank's banking business, on or before the date of the winding-up order, which are expressly exempted under section 468(2).[238]

4.2.4 Shareholders and liquidation

The transfer of shares or the alteration of status of shareholders in a company during liquidation will not be effective unless either the court permits or the Liquidator grants his/her written consent.[239] Any transfer of shares or alteration in the status of shareholders is dependent upon whether the Liquidator or the Court is satisfied that it is in the best interest of the company's creditors as a whole and that it does not breach any other sections of the Corporations Act that deal with the rights of shareholders.[240] There are certain conditions that the Liquidator can impose that must be satisfied when giving consent to a transfer of shares in a company or for the alteration of status of shareholders before the transfer or alteration is effective.[241]

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236 Section 468(1).
237 *Bona fides* is Latin for good faith. Hiemstra & Gonin (2012) 161.
238 The Corporations Act 50 of 2001, s 468(2).
239 Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).
240 Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).
241 The Corporations Act 50 of 2001, s 468A.

In the case of a transfer of shares, the affected shareholder or prospective shareholder or creditor may apply to the court to set aside any or all of these conditions. The same applies to a shareholder or a creditor for an alteration in the status of shareholders. Application to the court may be made to set aside any or all conditions that must be satisfied for an alteration in the status of shareholders to be effective. Similarly, a shareholder or a creditor may also apply to the court to grant or authorise an alteration in the status of shareholders if the Liquidator is not willing to grant the alteration.[242]

The Liquidator is entitled to call upon the holders of any unpaid or partly paid shares in the company to pay the outstanding amount on those shares. If the Liquidator makes a written declaration that he / she has reasonable grounds to believe that there is no prospect that the shareholders will receive any further distribution in the winding-up, the shareholders can realise a capital loss. The shares in the company must have been purchased either on or after the 20 September 1985 in order to realise a loss. If no declaration is made by the Liquidator, the dissolution of the company at the end of the winding-up process will also enable the realisation of any capital loss.[243]

4.2.5 Shareholders and voluntary liquidation

Voluntary administration is aimed at resolving a company's future direction swiftly. An independent and appropriately qualified person - the voluntary administrator - takes full control of the company with the aim of working out a way to either save the company or the company's

[242] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

[243] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

business. If this is not possible, the aim is to administer the company affairs in such a way that results in a better return to the company creditors than they would have received had the company rather been placed into liquidation. The instrument for achieving these aims is a deed of company arrangement.[244]

Shareholders do not get to vote on the future of the company and a voluntary administrator is not obliged to report to shareholders on the progress or outcome of the voluntary administration. Like in a court-ordered liquidation, the transfer of shares in a company or alteration of the status of shareholders during a voluntary administration will not be effective unless the voluntary administrator gives his/her written consent or the court grants permission. Similarly, the voluntary administrator or the Court will need to be satisfied that the transfer of shares or the alteration in the status of shareholders is in the best interest of the company's creditors as a whole and does not breach other sections of the Corporations Act relevant to the rights of shareholders.[245]

The voluntary administrator can impose conditions which must be satisfied before the transfer of shares or alteration of the status of shareholders is effective when giving his/her written consent to a transfer of shares in a company or alteration of status of shareholders. In the case of a transfer of shares the affected shareholder, or the prospective shareholder or a creditor may apply to the court to set aside any or all conditions and similarly a shareholder or a creditor may apply to the court to set aside any or all conditions that must be satisfied for an alteration in the status of shareholders to have effect. A shareholder or a creditor may also apply to the

[244] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

[245] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

court to grant an alteration in the status of shareholders if the voluntary administrator declines the alteration.[246]

The deed of company arrangement which is approved by the creditors binds the shareholders. The deed administrator is allowed to transfer shares in the company either with the written consent of the shareholder concerned or with the court's authorisation. A shareholder, a creditor, ASIC or any other interested person is allowed to oppose an application to the court by the deed administrator to approve a share transfer. If the deed administrator makes a written declaration that there is reasonable ground to believe that there is no possibility that shareholders will receive any further distribution at any time in the future, shareholders can realise a capital loss. To realise this loss the shares in the company must have been purchased on or after the 20 September 1985.[247]

4.3 THE BRITISH EXPERIENCE

Transferability of company shares tends to be taken for granted in listed companies, but when it comes to wholesale transfer of shares to a single person it becomes controversial in the form of a takeover bidder.[248] In such a situation the transfer of the shares has clear implications for the control of the company. By contrast in non-listed companies even the transfer of shares by a single shareholder may have ramifications for control of the company and often for its management, since a shareholding in such a company may be regarded as giving rise to a

[246] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

[247] Australian Securities and Investment Commission 'Insolvency: a guide for shareholders' available at *http://asic.gov.au/regulatory-resources/insolvency/insolvency-for-shareholders/insolvency-a-guide-for-shareholders/* (accessed 19 September 2017).

[248] Davies PL & Worthington S *Principles of Modern Company Law* 10 ed (2016) 894.

formal or informal entitlement to membership of the board of directors and involvement in the management of the company.[249] It is therefore common practice in such companies for the articles of association to contain some restrictions on the transferability of company shares.

This can be done by making transfer subject to the authorisation of the board or requiring the shares in the first instance to be sold to other shareholders before it can be sold outside the existing shareholder body.[250] The latter obligation is commonly referred to as giving other shareholders pre-emption rights arising out of transfer.

4.3.1 Transfer of shares and restrictions on transferability

The transfer of shares involves a two-step process. The first step involves the seller and purchaser concluding a sales contract where both parties agree on a sale price and on other terms of the transaction. This first step is often referred to as "trading" by bankers.[251] The second step is when the transfer is carried out at the end of which the purchaser becomes the owner of the shares that formed part of the sale transaction. This step is often referred to as "settlement" and is a process in which, itself, consists of two or more stages depending whether you are dealing with the sale of certificated or uncertificated shares. These sales transactions are completed by way of delivering transfer documentation from the seller to the purchaser and by way of registering the purchaser's name in the company securities register.

[249] Refer to Davies & Worthington (2016) 661 and 894, "In the case of an informal entitlement, it may be protected by the unfair prejudice remedy. The statutory unfair prejudice provisions are wide-ranging, the first of which can be found under Section 994(1) in Pt 30 of the British Companies Act 2006, which provides that any member may petition the court for relief on the ground: "(a) that the company's affairs are being or have been conducted in a manner which is unfairly prejudicial to the interests of members generally or some part of its members (including at least himself), or (b) that an actual or proposed act or omission of the company (including any act or omission on its behalf) is or would be so prejudicial."; The Companies Act 2006 (c46) is an Act of the Parliament of the United Kingdom which forms the primary source of UK company law.

[250] Davies & Worthington (2016) 894.

[251] Davies & Worthington (2016) 894.

In the United Kingdom (UK) the process of transferring certificated shares is completed when the seller completes a transfer form and delivers the transfer form together with the share certificate to the purchaser.[252] The transfer form needs to comply with either the requirements contained in the articles of association of the company or with the more simplified requirements put in place by the Stock Transfer Act.[253] This does not make the transferee a shareholder of the company nor will it pass legal title by either the agreement to transfer or the delivery of the signed transfer form and share certificate. It will however confer an equitable interest in the shares to the transferee.[254]

The rule is that the transferee becomes a member of the company and legal owner of the shares when his name is registered in the company's register of members. So the company enters the transferee's name on the register of members in place of the transferor's name.[255] This also means that a share certificate is not a negotiable instrument and thus legal title does not pass by mere delivery of the certificate but upon registration of the transferee by the company.[256]

Often directors of non-listed companies are authorised by the company's articles to refuse to register transfers or there will be provisions affording other members or shareholders of the company rights of pre-emption. This gives other members or shareholders the right of first

[252] Davies & Worthington (2016) 897.
[253] Stock Transfer Act 1982.
[254] Davies & Worthington (2016) 897.
[255] Refer to Davies & Worthington (2016) 897 footnote 18 "And, it seems, what then occurs is a novation (i.e. the relationship between the company and the transferor is ended and is replaced by a new relationship between the company and the transferee) rather than an assignment of the transferor's rights to the transferee (*Ashby v Blackwell* (1765) 2 Eden 299 at 302-303; 28 E.R. 913 at 914; *Simm v Anglo-American Telegraph Co* (1879) 5 Q.B.D. 188 at 204; E. Micheler, "Legal Title and the Transfer of Shares in a Paperless World-Farewell Quasi-Negotiaility [2002] J.B.L 358). If this is the rule it is favourable to transferees, for in general on assignment the assignee is in no better position than was the assignor."
[256] Davies & Worthington (2016) 897.

refusal or even compulsory acquisition.[257] This does not however apply to listed shares because the Listing Rules require there to be no restrictions of the transfer of shares.[258] As mentioned a stock transfer form is the usual form for the transfer of shares in a private UK company and section 770 of the Companies Act[259] provides that a company may not register a transfer of shares in the company provided a 'proper instrument' has been delivered to it or one of the exceptions set out in section 770 applies.

Section 770 Registration of transfer reads as follows:

> "(1) A company may not register a transfer of shares in or debentures of the company unless –
>
> (a) a proper instrument of transfer has been delivered to it, or
>
> (b) the transfer
>
> (i) is an exempt transfer within the Stock Transfer Act 1982 (c.41), or
>
> (ii) is in accordance with regulations under Chapter 2 of this Part.
>
> (2) Subsection (1) does not affect any power of the company to register as shareholder or debenture holder a person to whom the right to any shares in or debentures of the company has been transmitted by operation of law."

4.3.2 The position of transferor and transferee prior to registration

It is of significant importance to establish the precise position of the transferor and the transferee pending registration of a transfer, specifically if there are restrictions on

[257] Refer to Davies & Worthington (2016) 899 "Acquisition by a company itself will, of course, be lawful only if it is able to comply with the conditions enabling a company to buy its own shares. Less usually, the provision may impose an obligation on other members to buy."

[258] Except for any restrictions imposed for failure to comply with a notice under the Companies Act 2006 s.793 (notice by company requiring information about interests in its shares): Listing Rules r2.2.4.

[259] The Companies Act 2006 (c46) UK.

transferability which may occur.[260] It is only when the transfer is registered that the transferor ceases to be a member and shareholder and the transferee becomes the member and shareholder and the beneficial interest is transferred. In the instance of a sale of certificated shares the transaction will normally go through three stages. The first is an agreement for the sale of the shares. The second is the delivery of the signed transfer form and the certificate by the seller and payment of the price by the purchaser. Lastly, is the registration of the purchaser's name in the shareholders' register.

The beneficial interest in the shares passes from the seller to the purchaser at stage two. "The seller then becomes a trustee for the purchaser and must account to him for any dividends he receives and vote in accordance with his instructions (or appoint him as his proxy)."[261] This however raises certain issues, the first of which arises at stage two when delivery of the documents may not necessarily be matched by payment of the full price. By example, the agreement may have allowed for payment to be made in instalments and the seller will then hold a lien on the shares as an unpaid seller.[262] This does not prevent an equitable interest from passing to the purchaser but in such an instance the court will not grant specific performance unless the seller's lien can be fully protected.[263]

The second issue arises whether the foregoing can apply when the articles provide for pre-emption rights and first refusal when a shareholder wishes to sell his shares. "In such a case

[260] Davies & Worthington (2016) 902.
[261] Davies & Worthington (2016) 902; See also *Hardoon v Belilios* [1901] A.C. 118 PC; distinguished in *Wise v Perpetual Trustee Co* [1903] A.C. 139 PC.
[262] Davies & Worthington (2016) 903 footnote 49 "The normal practice then is to provide that the transfer and share certificate shall be held by a stakeholder and not lodged for registration until released to the buyer on payment of final instalment."
[263] Davies & Worthington (2016) 903; See also *Musselwhite v Musselwhite & Sons* Ltd [1962] Ch. 964; *JRRT (Investments) Ltd v Haycraft* [1993] B.C.L.C. 401; *Michaels v Harley House (Marylebone*) [1997] 2 B.C.L.C. 166; *Stablewood v Virdi* [2010] EWCA Civ 865; [2010] All E.R. (D) 204.

the transferor (perhaps with the full knowledge of the transferee[264]) has breached the deemed contract under s.33 between him and the company and his fellow shareholders."[265] In the House of Lords case in *Hunter v Hunter*[266] the court made observations that the transfer would be 'wholly void', even as between the transferor and transferee. In later cases[267] however, the courts have refused to follow this but at any rate, if the price has been paid, then the transferee obtains the rights the transferor had.

In the case of *Cottrell v King*,[268] the claimant Mrs Cottrell sought declarations relating to ownership of shares in a company to which her late husband Mervyn Cottrell was in partnership with the defendant Mr King. Mr King counterclaimed for the same relief. The articles of the company contained pre-emption provisions as follows:

"Article 12(a) of the company provides that no share or beneficial ownership of a share shall be transferred unless and until the rights of pre-emption contained in the articles have been exhausted.

Article 12(b) provides that any member proposing to transfer any share or beneficial ownership of a share (referred to as the 'vendor') shall give notice in writing (a 'transfer notice') to the company. The transfer notice is to specify the sum which in the vendor's opinion constitutes a

[264] As in Lyle & Scott Ltd v Scott's Trustees [1959] A.C. 763 HLSc.
[265] Davies & Worthington (2016) 903.
[266] *Hunter v Hunter* [1936] A.C. 222 HL.
[267] Refer to Davies & Worthington (2016) 903 footnote 54 "*Hawks v McArthur* [1951] 1 All E.R. 22; *Tett v Phoenix Property Co* [1986] B.C.L.C. 149, where decision on it at first instance was wrong. *Re Walls Properties Ltd v PJ Walls Holdings Ltd* [2008] 1 I.R. 732; *Cottrell v King* [2004] 2 B.C.L.C. 413; but see *Re Claygreen Ltd*; *Romer-Ormiston v Claygreen Ltd* [2006] 1 B.C.L.C. 715."
[268] *Cottrell v King* [2004] 2 B.C.L.C. 413.

fair price for the shares, and will constitute the company the vendor's agent for the sale of the shares to other members of the company at that price."[269]

Council for Mrs Cottrell alleged that the defendant waived his right of pre-emption and was involved in the transfer of shares into their client's name and argued that the defendant either knew or ought by reason of his office as director to have known of the pre-emption provisions. Mr King argued that he did not know about the pre-emption provisions and denied that he ought to have known of the pre-emption provisions and thus could not have waived his rights. He alleged that the transfer was the result of either a common or unilateral mistake and claimed that it should be either ineffective or be set aside.[270]

Council for Mrs Cottrell accepted that the pre-emption provisions applied in relation to the registration of the shares in their client's name. However, Mrs Cottrell's request triggered the pre-emption provision and argued that it was for the company to operate the provisions which it had not done. The court referred to the case of *Hunter v Hunter*, where the articles of the company contained a provision to the effect that no member was entitled to transfer shares unless notice is given to the company secretary and an offer in the first instance is made to the other shareholders in the company.[271]

One of the shareholders charged his shares to a bank and then following the charge he transferred the shares to nominees who in turn sold the shares and each transferee in turn being registered as a shareholder. One of the other shareholders in the company brought proceedings

[269] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).
[270] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).
[271] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).

to have the register rectified and the name of the original shareholder restored. The claim was successful at trial due to the fact that the articles prohibited a transfer. This decision was upheld by the court of appeal, the transfer and subsequent registrations being treated as inoperative.[272] There was no appeal to the House of Lords on this point, the appeal concerned a second action concerning different issues, but the court did regard the decision as correct.

Lord Atkin, held "the effect of [the article] in my opinion is to provide the means and the only means by which a member of the company can form an agreement for the sale of shares, which can only be constituted by the act of the secretary as agent for the seller and purchaser declaring a contract to be concluded at the price fixed by the auditor. This was not done in this case, and in my opinion no rights arose between the bank and [the ultimate transferee] under any contract of sale either equitable or legal."[273]

The case of *Tett v Phoenix Property and Investments Co Ltd*,[274] was concerned with a provision in the articles of a company that provided that no shares were to be transferred by a member of the company to a person not already a member of the company. In this case a shareholder had died and her shares were sold by her executors to the plaintiff who was not a member of the company, and without the pre-emption provisions being adhered to and thus the directors of the company refused to register the transfer.[275] It was argued in the basis of *Hunter v Hunter* that the transfer was in its entirety, void.

[272] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).
[273] *Hunter v Hunter* [1936] AC 222 at page 261.
[274] *Tett v Phoenix Property and Investments Co Ltd* [1984] BCLC 599.
[275] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).

Vinelott J, analysed the above statement made by Lord Atkin in the *Hunter* case, and concluded that:

"Lord Atkin took the view that the effect of [the pre-emption provision] was that no member could enter into a binding contract for the sale of his shares capable of conferring any interest legal or equitable on the purchaser unless and until he had given notice to the secretary, the secretary had offered the shares to the other members and none had accepted the offer within the time stipulated. However, the majority did not accept Lord Atkin's view that the transfer … was a nullity."[276]

Vinelott J analysed the legal effect of what had occurred in the case before him as follows:

"… the other members' rights to require [the deceased's] executors to offer the shares to them before transferring them to the plaintiff matured into an option to purchase the shares at the fair value to be determined by the auditors when the transfers were executed and that … option created an equitable interest prior in time to the interest taken by the other plaintiff under the transfer. Until registration the equitable interest of the other members in the shares would prevail over the subsequent interest of the plaintiff whether the members had notice of his interest or not.[277] After the registration of the plaintiff as holder of the shares in question the priority of the option would depend on whether the plaintiff had notice actual or constructive that the pre-emption provisions had not been completed with at the time when the transfer was executed."[278] The plaintiff in that case was a purchaser for value and in the case the decision was reversed on appeal but not on this point.[279]

[276] [1984] BCLC 599 at p.618a.
[277] *Tett v Phoenix* (1984) at p.619e; See also *Roots v Williamson* (1888) 38 Ch D 485.
[278] *Tett v Phoenix* (1984) at p.619e; See also *Dodds v Hills* (1865) 2 Hem & M 424.
[279] [1986] BCLC 149.

Under English law there seems to be two diverging opinions as regards the legality of a transfer in contravention of pre-emptive provisions. One of these views was expressed in *Tett v Phoenix* by Vinelott J. He observed that "Despite the disregard of pre-emption provisions there occurred a complete and effective transfer between transferor and transferee in terms of which the equitable title passes to the latter".[280] A company has a right to invalidate a transfer which is in breach of the provisions contained in the articles but once the company accepts a transfer in breach, it can no longer question the validity of such transfer. It follows that such a transfer is neither a nullity nor void *ab initio*.[281] The purchaser is therefore not left without remedy. The seller would thus be accountable to the purchaser for all growth such as dividend and bonus. Nonetheless, the court of appeal still maintained that the company would not be bound to such a transfer.

The position of the law in England with regards to this point, is that a transfer in contravention of pre-emption provisions is neither void nor illegal. It is a valid transfer in that the title of the share passes to the purchaser and the seller is liable for all growth to such share. Neither a company nor its shareholders are bound by such a transfer prohibited by the articles. This means that the company has a right to refuse a transfer in breach of pre-emption provisions of the company, however, if the company waives its right the transfer would be deemed valid. The shareholders can subsequently validate a transfer by their assent to the transfer.[282]

[280] All Answers ltd, 'Corporate Law Restrictions on Transferability' available at (Lawteacher.net, October 2018) <https://www.lawteacher.net/free-law-essays/company-law/corporate-law-i-final-draft-restrictions-law-essays.php?vref=1> (accessed 19 October 2018).

[281] All Answers ltd, 'Corporate Law Restrictions on Transferability' available at (Lawteacher.net, October 2018) <https://www.lawteacher.net/free-law-essays/company-law/corporate-law-i-final-draft-restrictions-law-essays.php?vref=1> (accessed 19 October 2018).

[282] All Answers ltd, 'Corporate Law Restrictions on Transferability' available at (Lawteacher.net, October 2018) <https://www.lawteacher.net/free-law-essays/company-law/corporate-law-i-final-draft-restrictions-law-essays.php?vref=1> (accessed 19 October 2018).

In applying the analysis of *Tett v Phoenix* to the case of *Cottrell v King*, the position of the judgment of the court was that Mrs Cottrell had become entitled to the shares as consequence of the death of Mr Cottrell. She elected to become holder of the shares rather than have the shares registered in the name of a nominee and she gave the company notice to this effect. The company could have rejected this but it did not. The effect of Mrs Cottrell giving notice to the company and her notice then treated as a transfer notice was to alter Mr King's right of pre-emption into an option to purchase the shares.[283]

The *Cottrelll v King* case was different to the position in the *Tett v Phoenix* case, as the legal title to the shares became vested in Mrs Cottrell the moment her name was registered in the shareholders' register but she was not a purchaser for value and accordingly took the shares subject to Mr King's equitable interest arising under the option. That equity still subsists and thus Mr King is therefore entitled to an order for rectification of the register as was ordered in the case of *Hunter v Hunter*.[284]

Equitable interest in England is a beneficial interest. Legal ownership is separate from beneficial ownership and as such a legal owner will not necessarily be the same as the beneficial owner.[285] It is said that the legal owner holds on trust the beneficial interest in the shares for the beneficial owner thus the beneficial owner will have the right to the income from the shares and the right to the proceeds of sale.[286] In other words, an equitable interest is an interest held

[283] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).
[284] Casemine 'Cottrell v King & Anor' available at *https://www.casemine.com/judgement/uk/5a8ff73860d03e7f57ea9de2#* (accessed 16 October 2018).
[285] Thompson Reuters Practical Law 'Beneficial interests in shares' available at *https://uk.practicallaw.thomsonreuters.com/3-202-2697?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1* (accessed 8 November 2018).
[286] Thompson Reuters Practical Law 'Beneficial interest in shares' available at *https://uk.practicallaw.thomsonreuters.com/3-202-*

by virtue of an equitable title, which title holds a beneficial interest in the shares that gives the holder the right to acquire formal legal title.

4.3.3 Winding up

The provisions for winding-up and dissolution of companies can be found almost exclusively in the British Insolvency Act 1986 and Pt IV of the Insolvency Rules and not in the Companies Act.[287] Once a company goes into liquidation, the difference between shareholders and creditors becomes somewhat more difficult to draw than usual.[288] The basic distinction with regard to the types of winding is between voluntary winding up and compulsory winding up by the courts.

4.3.4 Discretion of the Courts

British courts have a statutory discretion to refuse to grant a winding-up order on the grounds that some other remedy is available and if it seems that the petitioners are seeking this drastic option unreasonably. They also have inherent jurisdiction to refuse to grant an order for winding-up if in the opinion of the court the petitioners have brought a petition for an improper or unnecessary purpose.[289] On the other hand, if the purpose of the petition is legitimate then it does not matter if the motive of the petitioner is malicious.[290] If a winding-up order is made the

2697?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1 (accessed 8 November 2018).

[287] Insolvency Rules 1986 (SI 1986/1925) as amended on numerous occasions, and with the Insolvency Service planning a revised and consolidated version for 2016, in effect from 1 October 2016, details of which can be available at *http://www.legislation.gov.uk/uksi/2016/1024/contents/made* (accessed 14 May 2018).

[288] Davies & Worthington (2016) 1152.

[289] Davies & Worthington (2016) 1155; *Re Surrey Garden Village Trust Ltd* [1995] 1 W.L.R. 974 Ch; *Re JE Cade & Sons Ltd* [1992] B.C.L.C. 213.

[290] Davies & Worthington (2016) 1155; *Bryanston Finance Ltd v De Vries* (No.2) [1976] Ch. 63 CA.

first step is to appoint a Liquidator after which the company's affairs and property will pass to the Liquidator.

4.3.5 Timing of commencement of winding-up

The timing of commencement of winding-up is important as the winding-up order is deemed to have commenced as from the date the petition is presented.[291] If the winding-up order is made in respect of a company already in voluntary winding-up, then the winding-up is deemed to have commenced from the date of the resolution of winding-up voluntarily.[292] This dating back is important as it has the effect of invalidating property dispositions[293] and executions of judgments[294] which have been lawfully undertaken during the period between presentation of the petition and the order. If certain transactions are undertaken during this period they are liable to modification or circumvention in the event of winding-up or administration.[295]

4.3.6 Avoidance of property dispositions

In terms of section 127 of the British Insolvency Act the transfer of shares is void unless the court orders otherwise.[296] Section 127 'Avoidance of property dispositions' provides as follows:

[291] Davies & Worthington (2016) 1157.
[292] The Insolvency Act 1986, s129.
[293] The Insolvency Act 1986, s 127.
[294] The Insolvency Act 1986, s 128.
[295] The Insolvency Act 1986, sections 238-245.
[296] The Insolvency Act 1986, s 127.

> "In a winding up by the court, any disposition of the company's property, and any transfer of shares, or alteration in the status of the company's members, made after the commencement of the winding up is, unless the court otherwise orders, void."[297]

If one compares section 127 of the UK Insolvency Act to section 341 of the South African Companies Act of 1973 as set out in the transitional arrangements in Schedule 5 of the 2008 Act, one will determine that the two provisions are similar in nature.

One needs to consider who is making the disposition in a share transfer. It is clear that it is the shareholder making the disposition and not the company as the shares being transferred is shareholder property and not company property. This would mean that the new purchaser would have a right of action to claim damages from the shareholder and not the company in the event the company is in the process of winding-up after the purchaser has bought the shares but before he is registered in the company's securities register as the new shareholder. One also needs to consider that the original shareholder may have known that the company would be liquidated before the shares were sold to the purchaser. If this can be proven, then the purchaser ought to have a claim for damages against the shareholder and not the company with regard to the misleading and deceptive conduct by the shareholder.

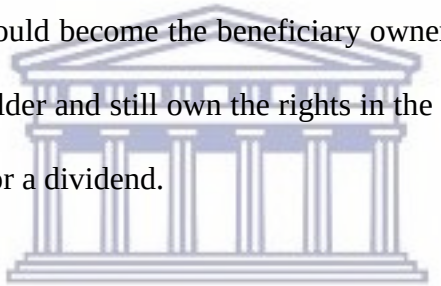
4.4 ANALYSIS IN LIGHT OF THE SOUTH AFRICAN POSITION COMPARED TO AUSTRALIA AND BRITAIN

As we have learned the transferability of shares executed after the commencement of the winding-up process under South African law is left to the discretionary decision made by the

[297] Section 127 of the Insolvency Act 1986; *Akers and others v Samba Financial Group* [2017] UKSC 6 page 2 para 7.

Liquidator. This is in terms of the transitional arrangements as set out in Schedule 5 of the 2008 Companies Act. Chapter XIV section 341(1) of the repealed 1973 Act remains in force.[298] Section 341(1) makes it clear that every transfer of shares that occurs at the starting point of the winding-up of a company is void, resulting in the person who acquired the shares becoming the beneficiary owner of the shares but does not acquire the legal rights to the shares.

In *Smuts v Booyens,* the court held that even though the cession of the shares would render the cessionary the owner of the share, the cessionary will not be regarded as a shareholder for the purposes of enforcing a right against the company. That depends, if cession occurred against a *pactum de non cedendo,* cession would be void and there can be no ownership that passes. In other words, the cessionary would become the beneficiary owner of the share and the cedent would still remain the shareholder and still own the rights in the share and thus be allowed to vote at meetings and qualify for a dividend.



Thus in order for the cessionary to acquire the rights in the shares other steps of transfer would have to be followed such as registering the new owner in the company's securities register. It is only once the purchaser is registered as the shareholder in the company's securities register does he acquire the rights and be able to exercise the right that is attached to the share. Under section 8(2)(b) private companies must restrict the transfer of its shares and the effect of such restriction, if not complied with, is that the shares are not transferable at all.[299] In *Smuts v Booyens* it was held that this is an absolute restriction.[300]

[298] Schedule 5 Chapter XIV of the Companies Act 71 of 2008.
[299] Section 8(2)(b) of the Companies Act 71 of 2008.
[300] *Smuts v Booyens* (2001) para 19.

This defining characteristic is not only applicable to South African company law but to Australian and British company law as well. Under Australian company law many proprietary companies contain pre-emptive rights which necessitate that a transferor offers his shares for transfer to other shareholders first before those shares can be offered to third parties.[301] Very often these constitutions will also give the directors the right to deny the registration of a share transfer without requiring them to provide a reason for such denial. Pre-emptive rights provisions are less common in public company constitutions however shareholders' agreements may provide restrictions on the transfer of shares. These types of restrictions are more typically expressed to take superiority over restrictions found in the company's constitution.[302]

The question of whether a transfer of shares would be invalid in instances of a breach of pre-emption provisions of a company's constitution during a winding-up process was raised in *Rathner v Lindholm*. The argument in this case was that the defendants were not entitled to the shares as the interest in the shares were transferred to the plaintiff. The counter argument by the defendants was that the plaintiff was not entitled to the shares as the transfer was a breach of the company's pre-emption provisions.

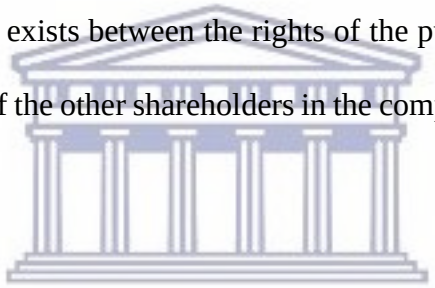
The court held that there had been an assignment of the shares to the plaintiff and that the plaintiff had an equitable proprietary interest in the shares. The issue was, did the assignment of the shares contravene the pre-emption provisions of the other shareholders and what the effect of such contravention would be. A transfer in contravention of a company's constitution

[301] McCormack J DLA Piper 'Guide to going global Corporate Australia' available at *https://www.dlapiperintelligence.com/goingglobal/corporate/index.html?t=38-restrictions-transferability-of-shares&c=AU* (accessed 7 June 2018).

[302] McCormack J DLA Piper 'Guide to going global Corporate Australia' available at *https://www.dlapiperintelligence.com/goingglobal/corporate/index.html?t=38-restrictions-transferability-of-shares&c=AU* (accessed 7 June 2018).

is wholly void but the court noted that there was a trend in modern authorities that was contrary to this approach.

After engaging in an analysis of case law dealing with this issue, Whelan J confirmed that historically the courts have held that a transfer in contravention of pre-emptive rights is ineffective and unenforceable.[303] In *Hawks v Mc Arthur*, it was held that the purchaser holds an equitable interest in the shares and Vaisey J, held that the transaction is not a complete nullity.[304] The competing interest was not between the purchaser and the shareholder but rather between the purchaser and parties with a competing equitable interest in the shares. Thus the equitable interest of the purchaser would prevail over a competing equitable interest second in time.[305] That said, if a conflict exists between the rights of the purchaser and the rights of the other shareholders, the rights of the other shareholders in the company would succeed over that of the purchaser.



Whelan J noted that a seller who transfers his shares in breach of pre-emption provisions cannot count on this breach to evade the contract but that the purchaser is not so prohibited and thus may avoid the contract on this basis. In the writer's opinion this would imply that the purchaser has a right to claim damages from the selling shareholder. Whelan J also noted that even though the purchaser has an equitable right in the shares the other shareholders would not be bound by the transfer and that the directors have the authority to deny registration of the transfer.[306] In the event the transfer is registered the shareholders may request that the registration be reversed.

[303] *Hunter v Hunter* [1936] AC 222.
[304] [2005] VSC 399 para 80; [1951] 1 All ER 22 and 27.
[305] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.
[306] *Rathner v Lindholm* (2005) VSC 399; Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.

In the United Kingdom it is common practice for private companies to contain restrictions on the transferability of shares in the articles of association. This can be done by making transfer subject to pre-emption rights arising out of transfer and by making transfer subject to authorisation by the board. In *Hunter v Hunter*, it was held that a transfer in breach of pre-emption provisions is 'wholly void'.[307] However, there is two diverging opinions one of which was expressed in *Tett v Phoenix*. Even though the pre-emption provision was not adhered to there was still a complete and effective transfer between the transferor and transferee in terms of which the equitable title passes to the transferee.[308] The purchaser is therefore not left without remedy and the seller would be accountable to the purchaser. This was the opinion of Vinelott J, however, the court of the appeal still maintained that the company would not be bound to such a transfer.

4.5 CONCLUSION

South Africa, Australia and Britain all seem to have similar provisions regarding the transfer of shares of a company being wound-up or alteration in the status of its shareholders after the commencement of the winding-up, in that without the sanction of the Liquidator, the transfer or alteration is void. Under South African law and with particular reference to *Smuts v Booyens* which is still the leading authority on this particular issue there is an absolute restriction, in that, if the restriction with regard to the transferability of company shares of private companies are not adhered to the transfer is void.[309]

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[307] *Hunter v Hunter* [1936] A.C. 222 HL.

[308] All Answers ltd, 'Corporate Law Restrictions on Transferability' available at (Lawteacher.net, October 2018) <*https://www.lawteacher.net/free-law-essays/company-law/corporate-law-i-final-draft-restrictions-law-essays.php?vref=1*> (accessed 19 October 2018).

[309] *Smuts v Booyens; Markplaas (Edms) Bpk v Booyens* 2001 (4) SA 15 [SCA].

The distinction in Australian law from South African law is that even though historically the courts have held that a transfer in contravention of pre-emptive rights is ineffective and unenforceable, modern authorities are of the view that a purchaser would still acquire the equitable proprietary interest in the shares and thus the transaction is not a complete nullity. As such a purchaser's equitable interest would prevail over a competing equitable interest second in time. In other words, the competing interests are not between the purchaser and the shareholder but between the purchaser and parties with a competing equitable interest in the shares. Also a seller who sells his shares in contravention of a pre-emption provision cannot rely on such contravention to evade the contract, a purchaser is not so prohibited and could avoid the contract on such basis. However, that said, the purchaser would not prevail over the interest of the other shareholders in the company.

The distinction in the United Kingdom from South African is that under English law in instances of contravention of pre-emption provisions there is still a complete and effective transfer between the transferor and the transferee in terms of which the equitable title passes to the transferee. As such the purchaser is not without remedy and the seller would be accountable to the purchaser. In general courts still maintain that a company would not be bound to such a transfer. In both Australia and the United Kingdom, it would seem that the purchaser would have a right to claim damages from the selling shareholder.

CHAPTER 5

CONCLUSION

5.1 INTRODUCTION

The aim of this study was to highlight the problems pertinent to the transfer of shares during a liquidation process and possibly provide a solution that will engage corporate contractual principles by contributing new knowledge and further enrich South African jurisprudence. This thesis explored the meaning of transfer of shares in terms of the common law, the 1973 and 2008 Companies Act and how the courts view what transfer is today. It analysed various sections of both the Companies Act of 1973 and 2008 as well as schedule 5 of the 2008 Act with regard to the transfer of shares in the course of a liquidation process of a company.

Borrowing from other jurisdictions is critical to improving the interpretation and understanding of South African law. English company law principles have had a long-standing relationship with South African company law.[310] Much of the legal framework and general principles of South African company law is still currently based on English law.[311] Australian company law also has much in common with that of South African company law as both jurisdictions include corporate insolvency provisions in its general company law statutes.[312]

As such reference to the legal framework of the United Kingdom and Australia will add value to the interpretation of South African company law as both comparators of choice are common law jurisdictions like South Africa and therefore well suited for this study. The decision to

[310] Government Gazette No. 26493 (Notice 1183 of 2004) 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform' 3.
[311] Anderson C 'Viewing the proposed South African Business Rescue provisions from an Australian perspective' (2008) *PER* 2.
[312] Anderson C 'Viewing the proposed South African Business Rescue provisions from an Australian perspective' (2008) *PER* 2.

modernise South African company law by the Department of Trade and Industry was aimed at bringing our law in line with international trends. It did not, however, provide clarity in the area of transfer of shares and the research problem, in a manner which reflects the principles and standard of South African's new corporate law reform.[313]

5.2 FINDINGS

The research problem was to determine what recourse a purchaser has, if any, in the event a transfer of shares is executed after the commencement of the winding-up process of a company, as the purchaser's rights to the shares are left to the discretionary decision by the Liquidator as illustrated by section 341(1) of the 1973 Act which still remains in force.[314] While the transfer of shares plays an important role in corporate law, before the 2008 Act came about this issue was illustrated in *Smuts v Booyens*, which today still remains the leading authority on this matter.

In South Africa, shares are generally freely transferable. Shareholders have the right to deal freely with their shares but in terms of section 8(2) (b) of the Act a private company's MOI must prohibit the offering of any of its securities to the public and restrict the transferability of its securities.[315] It is also possible for the MOI of a public company to contain transfer restrictions. The effect of non-compliance with this restriction in terms of the *Smuts v Booyens* case is that the transfer of shares is ineffective and void.[316]

[313] Government Gazette No. 26493 (Notice 1183 of 2004) 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform' 5.
[314] The Companies Act 61 of 1973, s 341(1).
[315] The Companies Act 71 of 2008, s 8(2)(b).
[316] *Smuts v Booyens* (2001) para 3.

The relationship between shareholders under the 2008 Companies Act is the same now as it was at the time of *Smuts v Booyens* and the 1973 Act and therefore the problem still exists. As such, in terms of South African corporate law there seems to be no remedy for a purchaser to whom shares have been transferred, unless that transfer took place before the winding-up process started.

Like South Africa, the United Kingdom and Australian company law have similar rules regarding the transferability of private company shares in a winding-up process. Section 468A of the Australian Corporations Act regulates the transfer of shares in a company that is made after the commencement of a winding-up by the Court, which provides that in such an instance the transaction is void.[317] Section 468(1) regulates company dispositions, any transfer of shares or alteration in the status of company members after the commencement of the winding-up by the court is void unless the court orders otherwise.[318] As such the law restricts the transfer of shares.

In Australia a transaction in contravention of pre-emption provisions is ineffective and unenforceable, however modern authorities are of the view that a purchaser would still acquire the equitable proprietary interest in the shares and thus the transaction is not a complete nullity. This is because a purchaser's equitable interest prevails over a competing equitable interest second in time.[319] A seller who sells his shares in contravention of a pre-emption provision will not be able to rely on such contravention to avoid the contract but a purchaser is not so prohibited and thus could avoid the contract on such basis. This is not the case however when

[317] The Corporations Act 50 of 2001, s 468A.
[318] The Corporations Act 50 of 2001, s 468(1).
[319] Blake A & Thomas B Equity and assignment of interest in contravention of pre-emptive rights (2006) 25 *ARELJ Victoria* 30.

dealing with the rights of the other shareholders in the company. The interest of the other shareholders will still prevail over the interest of the purchaser.

In the United Kingdom, the transferability of company shares in a winding-up is regulated by section 127 of the British Insolvency Act which provides that any transfer of shares or alteration in the status of company members made after the commencement of a winding-up is void, unless the court orders otherwise.[320] In the United Kingdom when dealing with the contravention of pre-emption provisions a complete and effective transfer between the transferor and the transferee occurs in terms of which the equitable title passes to the transferee.

This equitable interest in the United Kingdom can be defined as a beneficial interest. Legal title is separate from beneficial title.[321] It is said that the legal owner holds on trust the beneficial interest in the shares for the beneficial owner thus the beneficial owner will have the right to the income from the shares and the right to the proceeds of sale.[322] Thus the purchaser is not without remedy. In both Australia and England, it would seem that the purchaser would be entitled to claim damages from the selling shareholder.

From the analysis made in the three jurisdictions it would seem that it is common practice for the MOI in private companies to place restrictions on the transferability of company shares. This can happen in two ways, namely by means of pre-emptive rights extended to existing shareholders or by making transfer subject to the authorisation of the board of directors. The

[320] The Insolvency Act 1986, s 127.
[321] Thompson Reuters Practical Law 'Beneficial interests in shares' available at *https://uk.practicallaw.thomsonreuters.com/3-202-2697?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1* (accessed 8 November 2018).
[322] Thompson Reuters Practical Law 'Beneficial interest in shares' available at *https://uk.practicallaw.thomsonreuters.com/3-202-2697?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1* (accessed 8 November 2018).

process of transfer is the same in all three jurisdictions and the new purchaser of the shares only acquires the rights in the shares upon registration in the company's securities register. However, the in the United Kingdom is that until such time as the new purchaser is registered the seller of the shares becomes a trustee for the purchaser and must account to him/her for any dividends he receives and vote in accordance with the instructions of the transferee.[323]

This can raise certain issues, by example, the agreement may have allowed for payment to be made in instalments in which case the seller would hold a lien on the shares as an unpaid seller. This does not prevent an equitable interest from passing to the purchaser but in such an instance the court will not grant specific performance unless the seller's lien can be fully protected.[324] The court has held in *Hunter v Hunter* that the transfer would be 'wholly void', even between transferor and transferee.[325]

In South Africa the position is the same. If cession of shares has taken place and provided there is no *pactum de non cedendo*, the purchaser will become the beneficial owner and the seller will have to account to him for all dividends and voting rights. This was held in the case of *Standard Bank v Ocean Commodities,*[326]

"In some instances, however, the registered shareholder may hold the shares as the nominee, i.e. agent, of another, generally described as the "owner" or "beneficial owner" of the shares. The term "beneficial owner" is, juristically speaking, not wholly accurate, but it is convenient

[323] Davies & Worthington (2016) 902.
[324] Davies & Worthington (2016) 903.
[325] *Hunter v Hunter* [1936] A.C. 222 HL>
[326] *Standard Bank of South Africa Ltd and Another v Ocean Commodities Inc. and Others* [1983] 1 All SA 145 (A).

and well-used label to denote the person to whom, as between himself and the registered shareholder, the benefit of the bundle of rights constituting the share vests."[327]

5.3 RECOMMENDATIONS

In South Africa there seems to be no remedy for the plight of a purchaser with regard to the transfer of securities in the course of a liquidation process of a company. In South Africa, United Kingdom and Australia the law is the same in that the transferability of company shares in a winding-up is void. However, in Britain and Australia this is not an absolute restriction and the transaction will not be a complete nullity. However, giving the purchaser an equitable interest seems to apply under normal circumstances. If transfer of company shares have taken place after the winding-up process has already commenced the transaction is void unless the court provides otherwise, as provided for in sections 468A and 468(1) of the Australian Corporations Act and section 127 of the Insolvency Act in the United Kingdom. This does of course mean that the purchaser would have a right to claim for damages against the selling shareholder.

The problem in South Africa in terms of a private company is that the company has to write restrictions into its MOI when dealing with the transferability of company shares. If a transfer of shares happens against a *pactum de non cedendo*, the transfer is void. Whether liquidation takes place or not is immaterial as the purchaser will not become the owner of the shares. Since there is no cession, there can be no transfer and as a consequence the purchaser will not become the new shareholder. In other words, according to common law under the law of cession in

[327] [1983] 1 All SA 145 (A) at page 152.

South Africa, if there is a *pactum de non cedendo*, the cessionary cannot or does not become the owner at all and the cession is void, and if there is no cession there cannot be a transfer.

It is for this reason that the purchaser has no claim against the company. Like in Australia and the United Kingdom the purchaser will however have recourse against the person who sold him the shares. One of the implied obligations in terms of the law of contract between a buyer and seller is that the seller owes the buyer a duty of performance. Thus the seller would have to ensure that the purchaser becomes the owner of the shares and then subsequently become the shareholder in the company. Thus the purchaser would have the right to sue the person from whom he bought the shares.

It is important to bear in mind that if transfer takes place before winding-up the transaction will go ahead and the purchaser will be registered in the company securities register. However, if transfer occurs after winding-up has commenced it would not be in the best interest of the purchaser to be registered in the company's securities register. The date on which the transfer takes place is important but if transfer takes place after winding-up this date becomes immaterial as transfer will be void in terms of the restriction contained in the MOI of a private company. As such the liquidation process will have no effect either as cession will not have taken place and thus transfer cannot take place due to the *pactum de non cedendo* which exists.

In terms of the law of cession, one of the requirements for a valid cession is that the right being ceded is capable of being transferred, the general rule being that all personal rights are transferable.[328] That said, there are exceptions to this rule, one of which is the *pactum de non*

[328] Abrahams E *The Pactum De Non Cedendo: Through a Constitutional Lens* (unpublished LLM Thesis, The University of Cape Town, 2017 pp 11); Sharrock R 'Business Transactions Law' 8ed (2011) *Juta & Company Ltd* pp 252-254.

cedendo. A *pactum de non cedendo* can be defined as a clause which prohibits the transferability of a right by means of cession.[329]

In the leading case *Paiges v Van Ryn Gold Mine Estates Ltd*[330] the current approach to *pactum de non cedendo* was discussed and it was held that a debtor has to show that they have an interest in the prohibition against cession. If the debtor can show this, then the *pactum de non cedendo* is valid and binding.[331] The personal right thus becomes non-transferable and a cession in breach of the *pactum de non cedendo* will be void.[332] The shareholders in a private company will always have an interest in the *pactum* In terms of recent case law dealing with *pactum de non cedendo*, such as the case of *Born Free Investments 364 (Pty) Ltd v Firstrand Bank Ltd*,[333] it was held that the cession of a right contrary to a *pactum* will be of no force or effect.[334] The court referred to *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd*,[335] in which case Thring J held the following:

"A *pactum*, that which relates to a right which was created *ab initio* as a non-transferable right, the *pactum* is valid and enforceable against the world because the right is simply inherently incapable of being transferred by anyone; and a cession of such a right contrary to the *pactum* will be putative, and of no force or effect, even if it is a so-called "involuntary" cession; in other words, it will bind even a trustee in insolvency or a liquidator of the creditor."[336]

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[329] Abrahams E *The Pactum De Non Cedendo: Through a Constitutional Lens* (unpublished LLM Thesis, The University of Cape Town, 2017 pp 11); Sharrock R 'Business Transactions Law' 8ed (2011) *Juta & Company Ltd* pp 252-254.
[330] *Paiges v Van Ryn Gold Mine Estates Ltd* 1920 AD 600; Sunkel KD 'A comprehensive suggestion to bring the pactum de non cedendo into the 21st century' (2010) Vol 21 *Stellenbosch Law Review* 463.
[331] *Paiges v Van Ryn Gold Mine Estates Ltd* 1920 AD 615.
[332] Paiges v Van Ryn Gold Mine Estates Ltd 1920 AD 617.
[333] *Born Free Investments 364 (Pty) Ltd v Firstrand Bank Ltd* [2014] 2 All SA 127 (SCA).
[334] [2014] 2 All 127 (SCA) para 9.
[335] *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C).
[336] [2008] (4) SA 510 (C) at 518H – 519C; *Born Free Investments v Firstrand Bank Ltd* (2014) para 9.

There is an implied obligation on the seller in terms of the law of contract to ensure that the purchaser becomes the owner of the shares and subsequently the shareholder in the company. If this does not happen due to the fact that the seller has transferred his shares contrary to a pre-emption right contained in the company's constitution, then the purchaser will have an action for damages under the law of contract. Thus the solution lies within the law of contract, by means of *restitution in integrum*[337].

5.4 CONCLUSION

The *Smuts v Booyens* case was decided under the 1973 Act and while section 20(1)(a) required a private company to restrict 'the right to transfer its shares', the 2008 Act differs in that it requires a private company to restrict the transfer of its securities.[338] This change in wording can have an impact on this issue. Since the restriction placed on the transfer of shares in a private company tends to be strictly interpreted it would be preferable to clearly express this matter in the company's constitution. However, it remains to be seen whether the courts would strictly apply the decision reached in *Smuts v Booyens* to section 8(2)(b)(ii)(bb) of the current Act.[339]

In terms of section 341 of the 1973 Act it is clear that it is the shareholder making the disposition in a share transfer and that the shares being transferred are the property of the shareholder and not the company. This would mean that the purchaser has a right of action to claim damages against the existing shareholder in the event the company is in the process of winding-up after the shares have already been ceded to the purchaser but before the purchase

[337] Return to previous legal position. Restoration to the original position which is a remedy of rescission coupled with restitution. Hiemstra & Gonin (2012) 281.
[338] Cassim (2012) 76.
[339] Cassim (2012) 76.

has been registered in the company's securities register. As previously mentioned when dealing with the transferability of shares in a private company in contravention of pre-emptive rights during the process of a winding-up, *Smuts v Booyens*, continues to be the leading authority and until such time when this issue is further analysed in court it will remain so. However, it is the hope of the writer that the recommendations made in this thesis will provide some relief to the plight of the purchaser.

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