Dispute Resolution

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When is oppression oppression?

In the recent judgment of *Technology Corporate Management (Pty) Ltd and Others v De Sousa and Another* (613/2017) [2024] ZASCA 29 the Supreme Court of Appeal (SCA) analysed and developed the law on the oppression of minority shareholders, and clarified the circumstances in which such relief could be obtained.

This is a matter of some practical importance: many private companies have only a few shareholders and directors (they are often one and the same), and the relationship between them may become difficult or even break down.

The case had a long history, and in its finding the SCA overturned a 2017 judgment which had been cited as an authority on this vexing issue.

A majority shareholder in the company was dismissed as an employee. He complained that because he was no longer employed, he was "*locked in*" to the company against his will because he was unable to dispose of his shares, but he was also excluded from participation in its management. He claimed he had lost confidence in the management of the company and went to court to force the minority to buy his shares – the High Court said they had to, but this was overturned by the SCA.

In principle, the parties had agreed to separate, but could not agree on the terms of the separation, particularly the price for the shares of the exiting shareholder. The court had to determine whether the minority shareholders should buy out the majority in order to force the issue.

The general principle is that the supremacy of the majority is essential to the proper functioning of companies. Minorities have to accept that steps taken which they do not like, or which may be unfavourable to them, generally bind them.

Legislation both here and overseas has recognised, however, that in certain circumstances, even if majority shareholders strictly adhere to the contractual terms governing the relationship, they may still act oppressively and be unfairly prejudicial against minority shareholders. In such circumstances the minority may approach the court for relief.

Understanding prejudice

Over the years, the courts have wrestled with what is meant by the concept of "*unfair prejudice*" – prejudice is inherently unfair, so when does it become actionable in the hands of a minority. The courts have therefore dealt with it as a concept to be applied to the particular facts of each case. The starting point is that the court should not interfere in the management of a company as a general rule but rather when the oppression becomes so unfair that intervention is required.

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As Wallis JA put it:

> *"Dissatisfaction and disagreement with, or disapproval of, the conduct of the business, does not of itself mean that the member has suffered unfair prejudice. The fact that there are irreconcilable differences between shareholders may in some circumstances justify an order for winding up the company, but it is not, without more, unfair prejudice. Something more is required. The question is, how much more?"*

Lord Hoffmann said this in an English case to which reference was made: *"Unfairness may consist in a breach of the rules [of a company] or in using the rules in a manner which equity would regard as contrary to good faith."*

Wallis JA noted that there are two, often overlapping, common factual situations where claims as to unfair prejudice usually arise:

> *"The first is where there was an agreement or understanding that all or some of the shareholders would participate in the conduct of the business, whether as directors or employees or both, where the unfair prejudice lies in their being prevented from doing so. These can conveniently be described as exclusion cases. The second is where, in the absence of such an agreement or understanding, the conduct of the majority shareholder, especially where it involves a lack of probity on their part, brings about a loss of trust and mutual confidence, but the disaffected shareholder is unable to address that by disposing of their interest in the company. The result is that they are effectively locked in and unable to realise the value of their investment."*

After analysing these situations with reference to case law, the court took the view that mere exclusion did not justify a right to exit where the business of the company could continue. A relationship breakdown – where the cause was not categorically a blameworthy fault on the part of one party – leading to a loss of trust was not enough to justify an exit. Wallis JA found that:

> *"It will almost always be prejudicial for the withdrawing minority shareholder to be unable to realise their investment. However, prejudice alone, and even a loss of trust in the majority, is not necessarily unfair. After all the minority shareholder agreed to become a shareholder on the basis that they could not freely dispose of their shares in the company. One of the risks of conducting a business with others in a small private company is that leaving the business and disposing of one's interest in it may be difficult or practically impossible. Small private companies in South Africa have always been required to have provisions in their articles of association restricting the transferability of shares. This is still the case under section 8(2)(b)(ii)(bb) of the [Companies Act 71 of 2008]."*

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And further:

> *"If claiming that one had lost faith in the majority were the key to unlocking a right to demand that the company or the majority acquire the minority's shareholding, it would effectively confer a right to exit the company at will at the expense of the remaining shareholders. A court should not allow a claim of unfair prejudice to be used to rewrite the terms on which the parties agreed to conduct the affairs of the company.*
>
> *To permit a shareholder to withdraw and compel either the remaining shareholders, or the company, to purchase their shares might imperil the future of the company and prejudice its creditors. Its shareholders would be prejudiced by being forced to dispose of assets or borrow money in order to pay the price fixed for the shares of the departing shareholder. It might even lead to the winding up of the company or the sequestration of the other shareholders. Allowing that to happen to a functioning and otherwise solvent business is not in the public interest."*

Conclusion

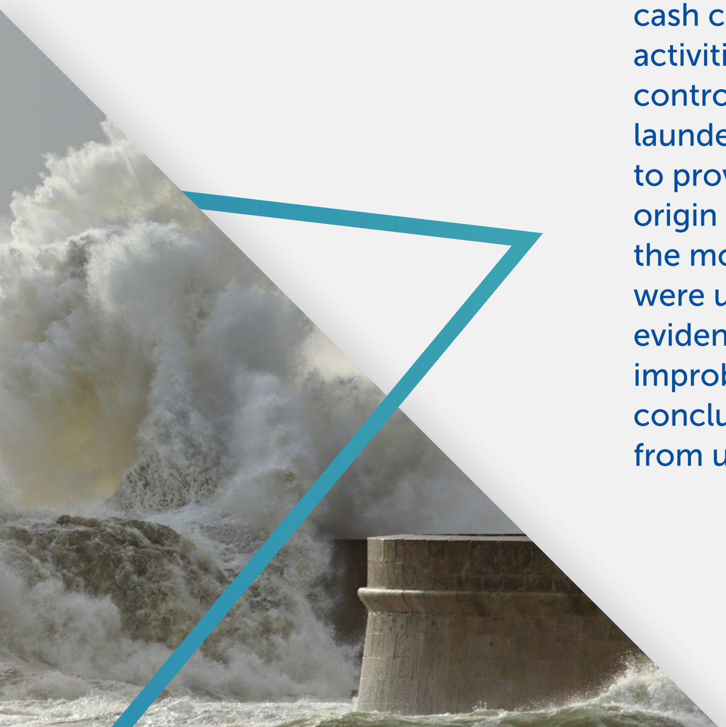
What the SCA has done has put the brakes on a developing legal trend that was making it easier for aggrieved shareholders to exit companies when they were dissatisfied with how they were being run, or with the conduct of their co-shareholders. If the majority, or those in control even if they are a minority, are acting within their powers both in the law and in terms of the arrangements amongst the shareholders have with each other, they will have to accept the position even if they believe it is bad for them and the company. Unfair oppression would only arise if the controllers stepped outside of these legal boundaries e.g. by paying a dividend to themselves and not a minority shareholder where the constitution of the company required otherwise, or in acting in a way that was demonstrably dishonest or broke the law.

An exit is not available for grumpy shareholders who don't like what the controllers are doing provided what the controllers are doing is lawful and within the company's constitutional and management rules.

Richard Marcus

Show me the money

In the case of *National Director of Public Prosecutions v Dhurgasamy* [2023] JOL 60116 (GJ), the National Director of Public Prosecutions (NDPP) applied for a forfeiture order under section 53, alternatively section 50 read with section 48, of the Prevention of Organised Crime Act 121 of 1998 (POCA). The application sought to declare certain property, specifically USD 630,700 in cash seized at OR Tambo International Airport on 11 September 2018, forfeit to the state. The Gauteng Division of the High Court in Johannesburg delivered judgment on 26 July 2023, granting the forfeiture order under section 50 of POCA. The court found that, on a balance of probabilities, the seized cash constituted the proceeds of unlawful activities, specifically violations of exchange control regulations and involvement in money laundering operations. The respondent failed to provide a credible explanation for the lawful origin of the funds, and his claims of obtaining the money through a loan for business purposes were unsubstantiated and lacked supporting evidence. The court noted inconsistencies and improbabilities in his account, leading to the conclusion that the funds were indeed derived from unlawful activities.



It must be noted that the NDPP is empowered by POCA to seek forfeiture of property deemed to be the proceeds of unlawful activities or instrumentalities of crime. In particular:

- Section 50(1) of POCA mandates the High Court to grant a forfeiture order if it is established on a balance of probabilities that the property is an instrument of an offence listed in Schedule 1 or the proceeds of unlawful activities.
- Section 50(5) of POCA requires the Registrar of the court to publish a notice of the forfeiture order in the Government Gazette.
- Section 25(1) of the Constitution provides that no one may be deprived of property except in terms of a law of general application, which raises questions of proportionality in forfeiture cases.

In *National Director of Public Prosecutions v Botha N.O.* [2020] ZACC 6 the court held that proceeds of crime are not protected as property under section 25(1) of the Constitution, reinforcing the state's ability to seek forfeiture orders. The NDPP contended that the seized cash constituted proceeds of unlawful activities, particularly violations of exchange control regulations.

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Conclusion

When it comes to big bucks and forfeiture fights, the stakes are always high. This case isn't just about who gets to keep the cash – it's a showdown between financial regulations and individual property rights. If the money talks, the law listens, and in this case, it's whispering *"proceeds of crime"*.

The case hinges on whether the state can prove on a balance of probabilities that the money is either proceeds of crime or an instrument of an offence under POCA. The proportionality principle, as discussed in *NDPP v Botha N.O.*, suggests that if property is deemed to be the proceeds of crime, forfeiture is mandatory. This case serves as a critical precedent in the enforcement of financial crime legislation and the constitutional interpretation of property rights in forfeiture matters.

Corné Lewis and Ledile Maloka

Battle of the insolvency provisions: Which law governs insolvency of insurance companies?

When a company hits a rough financial patch and is unable to make good on its financial obligations, liquidation serves as a valid legal mechanism available to creditors to recover debts owed to them. However, the liquidation of an insurance company presents unique challenges, underscored by the existence of two distinct laws enacted to address this process and an industry that must balance both private and public interests.

The business of insurance, although primarily a matter of private contract, is characterised as one that is vested in public interest, as was held in the case of *Commission on Administrative Justice v Insurance Regulatory Authority and Another* [2017] (eKLR). Consequently, it is subject to government regulation under the Insurance Regulatory Authority, whose main purpose is to protect the public as insurance consumers and policy holders. As such, the insolvency of an insurance company ought to be navigated in a manner that ensures the stability of the insurance sector, while simultaneously safeguarding the private interests of creditors. The question that then arises is: which of the laws enables the courts and stakeholders to achieve this outcome?

The criteria used to determine whether a company should stay in operation or undergo liquidation is the insolvency test, which is the legal and financial evaluation of an organisation's financial soundness, taking into consideration the company's assets, liabilities and compliance with regulatory solvency requirements.

The Insurance Act

On one hand, the Insurance Act, Cap 487, Laws of Kenya (Insurance Act) provides that the solvency of an insurance company ought to be assessed based on its adherence to the solvency margin outlined in section 41 of the Insurance Act. This margin, also known as the capital adequacy ratio, refers to the minimum excess on an insurer's assets over its liabilities, and is currently set at 100%. Consequently, if an insurance company does not meet the solvency margin, section 122 of the Insurance Act permits any person other than the Commissioner of Insurance to institute an application for liquidation against them. In line with this, section 61 of the Insurance Act requires all insurance companies to publish their annual balance sheets in at least two national newspapers at the end of the financial year.

A person who applies for the liquidation of an insurance company is also obligated by section 121 of the Insurance Act to join the Commissioner of Insurance, who serves as the CEO of the Insurance Regulatory Authority, as a party to that suit. The purpose of this is to enable the Insurance Regulatory Authority to carry out its mandate of regulating the insurance sector while simultaneously protecting the public as insurance consumers and policyholders.

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The Insolvency Act

One would assume that the insolvency of insurance companies would be governed exclusively by these provisions, considering the Insurance Act's tailored focus on the insurance industry. However, the ruling of Judge W.A Okwany in the case of *Salesio Kinyua Njagi and Nine Others v Invesco Assurance Company Limited* [2021] (eKLR) held otherwise.

In that case, the petitioners instituted liquidation proceedings against an insurance company pursuant to the provisions of the Insolvency Act, Cap 53, Laws of Kenya (Insolvency Act). They relied on the provision that permits a person to liquidate a company if it has not paid its debt of KES 100,000 within 21 days of it being demanded. According to section 384 of the Insolvency Act, a person can institute liquidation proceedings if a company is unable to pay its debts, meaning that:

- a company is indebted for KES 100,000 or more but has not paid the debt within 21 days of a demand being served upon it;
- a company is unable to pay its debts as they fall due; or
- the value of a company's assets is less than its liabilities.

However, the insurance company objected to this test, arguing that insolvency of an insurance company cannot be prosecuted under the Insolvency Act in isolation, and to the exclusion of the Insurance Act. The company also protested that the Commissioner of Insurance, who ought to be involved in liquidation proceedings of an insurance company for the protection of the insurance sector, was not involved in the proceedings.

Initial finding

However, the judge determined that there was nothing that excluded insurance companies from the operation of the Insolvency Act. She relied on section 3(2) of the Insolvency Act, which provides that the Insolvency Act applies to "*natural persons, partnerships, limited liability partnerships, limited liability partnerships, companies and other corporate bodies established by any written law*". Consequently, she held that by virtue of that section, a debtor could institute liquidation proceedings against an insurance company because an insurance company is a company as defined in that section. The petitioners were therefore granted the liquidation orders as sought, evidently protecting only the private interests of the petitioners and without due regard for the interests of the other policyholders or the protection of public interest.

Subsequent appeal

The petitioners then applied to have those liquidation orders set aside, claiming that the insurance company had since paid the debts owed to them. Justice A. Mabeya, who received the subsequent application to set aside the liquidation orders, expressed great concern about this process. In his ruling, he emphasised that once a petitioner has decided that a debtor company should be liquidated, it is insensitive for the petitioner to turn around and say, "*Oh, wait a minute, I have received my money back. Hold the process.*" This is because once an advertisement for liquidation has been made, as is required by law, the implications can cause irreparable harm by damaging the reputation of the insurance company, especially where it eventually pays its dues and the creditor no longer sees the

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need to have the company liquidated. Additionally, Justice Mabeya cautioned creditors against using liquidation proceedings to twist companies' arms to pay their debt, because the repercussions to the public are substantial.

Reversing the liquidation orders

In determining whether to lift the liquidation orders, Justice A. Mabeya took a different approach from the initial determination. He considered whether it was in the best interest of the public to keep the insurance company under liquidation and consequently reversed the liquidation orders on those grounds. He further emphasised that liquidation orders should only be issued if it is in the interest of the public and in all fairness not to let the company sink into further debt.

What is evident is that there is a discrepancy in the application of the law around insolvency of insurance companies. The sole application of the Insolvency Act overlooks the unique needs and complexities of the insurance industry that are in turn addressed by the Insurance Act. In fact, one may argue that an action to liquidate an insurance company on account of one creditor's private interests defeats the purpose of the insurance sector, as well as the function of the Insurance Regulatory Authority in preserving the sector.

Section 121 of the Insurance Act states that *"For the purpose of section 384 of the Insolvency Act (Cap. 53), an insurer is taken to be unable to pay its debts if at any time the requirements of section 41 (which relate to margins of solvency) are not observed by the insurer."*

Was the intention of this provision to remove insurance companies from the tests enshrined in section 384 of the Insolvency Act?

Conclusion

The question of which legal provisions should be applied to the insolvency of insurance companies is one that requires clarity and permanent resolve in order to create a more equitable legal environment for insurance companies and their clients.

Either way, creditors that are owed money by insurance companies have the alternative of pursuing debt recovery proceedings and attaching the assets of the company to recover sums owed. Taking this approach, as opposed to rushing to the extreme of liquidation proceedings, would create a more favourable outcome for all parties involved, since it would enable the creditor to recover their debt while maintaining the standing and reputation of the company and safeguarding the interests of the public in the insurance sector.

In conclusion, it is apparent that the interest of the public is of great concern to the insurance industry, necessitating its consideration when filing liquidation proceedings against such companies. It is imperative to have clarity on the law that ought to govern the prosecution of insolvency of insurance companies, to ensure that the process safeguards the integrity of the insurance sector while simultaneously protecting the private interests of creditors.

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