THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

JUDGMENT

Reportable

Case no: 483/2018

In the matter between:

CDH INVEST NV	**APPELLANT**
and	
PETROTANK SOUTH AFRICA (PTY) LTD	**FIRST RESPONDENT**
AMABUBESI INVESTMENTS (PTY) LTD	**SECOND RESPONDENT**
COMPANIES & INTELLECTUAL PROPERTY COMMISSION	**THIRD RESPONDENT**
MINISTER OF TRADE & INDUSTRY	**FOURTH RESPONDENT**

Neutral citation: *CDH Invest NV v Petrotank South Africa (Pty) Ltd & others* (483/2018) [2019] ZASCA 53 (1 April 2019)

Bench: Ponnan and Saldulker JJA and Davis, Carelse and Rogers AJJA

Heard: 1 March 2019

Delivered: 1 April 2019

Summary: Validity of directors resolution in terms of s 74 of Companies Act 71 of 2008 – the powers of directors when increasing the authorised shares of a company in terms of s 36(2)*(b)* and (3) of the Act.

ORDER

On appeal from: Gauteng Division of the High Court, Johannesburg (Van der Linde J sitting as court of first instance):

The appeal is dismissed with costs, such costs to include the costs of two counsel.

JUDGMENT

Carelse AJA (Ponnan and Saldulker JJA and Davis and Rogers AJJA concurring):

[1] This appeal concerns a decision adopted by written consent of the majority of the directors in terms of s 74 of the Companies Act 71 of 2008 (the Act).[1]

[2] The appellant (CDH) and the second respondent (Amabubesi) hold all the issued shares in the first respondent (Petrotank) in a 60/40 ratio. There are 100 000 issued shares. This accorded/was in accordance with a shareholders agreement (styled a MOI – MOU) concluded between the parties in January 2013. However Petrotank's memorandum of incorporation (MOI) of February 2013 mistakenly recorded the number of authorised shares as 1000. CDH sought an order in terms of s 61(12) of the Act directing the board of Petrotank to convene a shareholders meeting in terms of s 61(3) of the Act for the purpose of

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[1] Section 74 of the Companies Act 71 of 2008 provides:
'**Directors acting other than at meeting –**
(1) Except to the extent that the Memorandum of Incorporation of a company provides otherwise, a decision that could be voted on at a meeting of the board of that company may instead be adopted by written consent of a majority of the directors, given in person, or by electronic communication, *provided that each director has received notice of the matter to be decided*.' (My emphasis.)

considering and passing five resolutions: (1) the removal of a director; (2) the election of a substitute director; (3) instructing the board to demand that the minority shareholder, Amabubesi, pay Petrotank R1 million; (4) instructing the board to sue Amabubesi for this amount; and (5) instructing the board to consider a pro rata rights offer of 98 835 ordinary no par value shares.

[3] Amabubesi consented to the first two resolutions. Although the court a quo (Van der Linde J) dismissed the application in respect of the three remaining resolutions, the appeal to this court only concerns the dismissal of the application in respect of the fifth resolution.[2] Van der Linde J also upheld a counter–application by Amabubesi to invalidate a director's round robin resolution of Petrotank passed on 31 March 2014 that purported to amend its MOI by increasing the number of authorised shares from 1000 to 1 000 000. The declaration of invalidity of the increase of the authorised shares to 1 000 000 shares had the consequence that there were no additional authorised shares that could be utilised to conduct a rights offer.

The Facts

[4] In 2013 CDH, a Belgium company, and Amabubesi, an empowerment company, caused Petrotank, a partnership vehicle, to be incorporated. Petrotank's business included the manufacture of steel and petroleum storage tanks. The MOU provided that there would be five directors, three appointed by CDH and two by Amabubesi. At all material times the directors appointed by CDH were Messrs D'Hondt, Mabale and Stadler as managing

[2] *CDH Invest NV v Petrotank South Africa (Pty) Ltd & another* (22312/2015) [2017] ZAGPJHC 324; [2018] 1 ALL SA 450 (GJ); 2018 (3) SA 157 (GJ).

director. The directors appointed by Amabubesi were Messrs Moyo and Ntsaluba. Petrotank appointed Lucro Auditing as its auditors.

[5] Due to an error on the part of the person responsible for the incorporation of Petrotank, its MOI recorded that it had authorised shares of 1 000 ordinary no par value shares rather than 100 000. At the time CDH and Amabubesi were unaware of this error.

[6] On Tuesday, 25 March 2014, Moyo, of Amabubesi met with Stadler and Mabale, to discuss the business of Petrotank. On Wednesday, 26 March 2014, Moyo sent an email to Stadler and Mabale confirming what was discussed at the meeting.

[7] On Friday 28 March 2014 at 15h49 Stadler sent a detailed email to his fellow Petrotank directors in which he dealt extensively with the meeting of 25 March 2014. The email concluded:

‘ . . . Please also note that it came to my attention that Petrotank is in breach of the Companies Act, in that more shares are in issue than have been authorised. In order to rectify this position, I attach hereto various documents (including a directors’ resolution aimed at putting the Company on the “right side of the Companies Act.”

Therefore please tend [sic] to signature and return of the attached resolution, in order for us to rectify the situation.’

There is no explanation as to how, when or why this breach came to his attention.

[8] Attached to this email was a directors round robin resolution in terms of s 74 of the Act. The relevant portion of the resolution reads:

‘**Whereas** the Company is, via it[s] Memorandum of Incorporation, authorised to issue no more than 1 000 (one thousand ordinary) no par value shares; and

Whereas the current shareholders of the Company have agreed that 100 000 (one hundred thousand) shares will be issued amongst them (in a 60 000/ 40 000 split); and

Whereas it is a legal requirement, to ensure compliance with the Act as relates to authorised and issued shares that the Company's number of authorised shares be increased and the Company's Memorandum of Incorporation be subsequently and accordingly amended;

Now therefore be it resolved that, in terms of sections 36(2)(b) and 36(3) of the Act, the board herewith increases the Company's number of authorised shares to such an extent that the Company is authorised to issue no more than 1 000 000 (one million) ordinary no par value shares; and

Be it further resolved that, in terms of section 16(1) (b) of the Act, the Company's Memorandum of Incorporation be amended so as to delete and replace the current wording of clause 2.1(1) (but specifically excluding its sub-clauses (a) to (c) which remain) of the Memorandum of Incorporation with the following wording: *"The Company is authorised to issue no more than 1 000 000 (one million) ordinary no par value shares, and each such issued share entitles the holder to - ". . . '*

[9] On the same day at 22h05, Ntsaluba sent an email to all the directors stating that: 'In my capacity as a director, I will propose an investigation on this before I sign the documents. All my rights are reserved'. On Monday 31 March 2014, notwithstanding Ntsaluba's objection, the three CDH directors signed the round robin resolution. On Friday 4 April 2014, Mr Sontshaka, a legal advisor to Amabubesi, sent an email to Stadler that was copied to Moyo and Ntsaluba stating that: 'The current resolution requiring that the authorised shares be increased to 1 000 000 is incorrect and needs to be amended accordingly'. From the rest of the email it is apparent that the asserted error in the resolution was the fact that it increased the number of authorised shares to 1 000 000 instead of to 100 000 as agreed in the MOU. It is also apparent that Amabubesi's nominees on Petrotank's board were unaware

at this stage that CDH's nominees had already signed the impugned resolution. Both emails were ignored.

[10] Section 16 of the Act[3] provides that an amendment to the MOI of a company only becomes effective when it is filed with the Companies and Intellectual Property Commission (CIPC). Notwithstanding Amabubesi's emails pointing out the error, on 5 June 2014 D'Hondt, purporting to be duly authorised by Petrotank, applied to the CIPC to register the amendment to Petrotank's MOI to increase its authorised shares to 1 000 000. On 21 July 2014 the CIPC addressed a letter to Adendorff's Accounting, Tax & Secretarial Services (Adendorff) informing them that the amendment had been accepted and placed on file. It is not in dispute that the services of Lucro Auditing were not utilised to take the necessary steps to effect the amendment to the MOI. CDH has proffered no explanation for using the services of Adendorff instead of Lucro Auditing.

[11] More significantly CDH offered no explanation for its failure to have any regard to the objections raised by Amabubesi's directors to the round robin resolution. Amabubesi was unaware of the passing and registration of the resolution and thought the matter had been resolved.

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[3] Section 16 provides:
'**Amending Memorandum of Incorporation**. - (1) A company's Memorandum of Incorporation may be amended -
(a) . . .
(b) In the manner contemplated in section 36 (3) and (4)'
Section 36(3) provides -
'(3) Except to the extent that a company's Memorandum of Incorporation provides otherwise, the company's board may –
(a) increase or decrease the number of authorised shares of any class of shares.'
Section 36(4) provides:
'(4) If the board of a company acts pursuant to its authority contemplated in subsection (3), the company must file a Notice of Amendment of its Memorandum of Incorporation, setting out the changes effected by the board.'

[12] For reasons that need not be dealt with, the relationship between the parties had by April 2015 broken down. This was the month in which CDH delivered its demand that a shareholders meeting be convened to consider the five resolutions previously mentioned. The application giving rise to the present appeal followed on 22 June 2015. In July 2015 Amabubesi delivered, together with its opposing papers, the counter–application to which I have already referred.

The appeal

[13] The court a quo found that the resolution of 31 March 2014 was invalid because the three Petrotank directors who signed the resolution (ie the CDH nominees on Petrotank's board) had violated their fiduciary duty. The learned Judge considered that compliance with their fiduciary duty required that the power to increase the authorised shares be exercised in good faith and in the best interests of the company (a subjective test impeachable only on the limited grounds of irrationality) and for a proper purpose (an objective test). He considered that the CDH nominees' conduct failed on both legs. As to the first leg, the motivation provided for the impugned resolution was a devious misrepresentation because it failed to offer any justification for increasing the authorised shares to 1 000 000. The resolution was in any event irrational, having regard to the proclaimed purpose of correcting the error in the MOI. For similar reasons he found that objectively the resolution was not proposed and passed for a proper purpose. For the reasons which follow, I am in essential agreement with the court a quo though I believe a conclusion that the resolution was invalid can be reached on a somewhat narrower basis. It is thus unnecessary to consider the court a quo's extensive survey of Commonwealth authority.

[14] Two issues were raised by CDH's counsel on appeal: whether or not the court a quo's factual findings were based on a case that was never pleaded and whether or not there is any evidence that CDH's directors conducted themselves in a misleading fashion when they amended the MOI. For the first time in argument, CDH raised the issue that Amabubesi did not initially plead that the manner and the conduct of CDH's directors when it passed the resolution, which had the effect of amending the MOI, constituted a breach of their fiduciary duties or a misrepresentation. In counsel's view, this failure denied CDH the opportunity to deal with the allegations of corporate fraud against its directors.

[15] According to the appellant's counsel these allegations were made for the first time in reply when Amabubesi stated: '[t]he resolution was sent to the directors on 28 March 2014 and Stadler's email that accompanied it was deviously couched in a misleading fashion' and '[t]he proposed round robin resolution and accompanying emails was misleading'. CDH's counsel contended that what was not raised by Amabubesi in the court a quo was a case based on a breach of fiduciary duties or a misrepresentation in regard to the round robin resolution. Leave to appeal was not sought or granted on this issue.

[16] It is not correct that Amabubesi had only dealt with this issue in reply. In his answering affidavit, on behalf of Amabubesi, Moyo (whose affidavit also served as the founding affidavit to the counter–application) stated clearly that the demand relating to the rights issue was intended to harass, bully, oppress and unfairly prejudice Amabubesi and that CDH's directors were acting in 'gross bad faith'.

[17] It is common cause that the authorised shares would have had to be increased to 1 000 000 before the rights issue of 98 835 could be considered and it must be accepted that the issue of bad faith was pleaded in relation to the rights issue. As noted above, the two events were clearly linked and could not be separated as CDH's counsel sought to argue. In these circumstances, it cannot be suggested that Amabubesi sought to make out a case that was not raised in its founding affidavit to the counter–application.

[18] I now turn to deal with the question of misrepresentation by CDH. Section 36(2)*(b)* read with subsection (3) of the Act[4] contains a radical departure from the Companies Act 61 of 1973 (the Old Act). Whereas under ss 75 and 221 of the Old Act, a company could only increase its share capital by means of a special resolution and the directors required the company's prior approval at a general meeting before allotting or issuing shares, in terms of s 36(3) of the Act a company's shares can be increased or decreased by the board of a company, save to the extent that the MOI provides otherwise.

[19] In conducting the business of a company, directors can choose to do so at a formal directors' meeting where following deliberation they will pass a resolution that is immediately recorded. An alternative and more convenient means of conducting a company's business is by way of a round robin resolution as contemplated in s 74 of the Act. An important issue raised in this case is whether a director of a company is obliged to provide a justification when he or she proposes an increase in the authorised shares of a company by way of a

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[4] Section 36(2)*(b)* provides -
'(2) The authorisation and classification of shares, the numbers of authorised shares of each class … as set out in a company's Memorandum of Incorporation, maybe changed only by-
(a) . . .
(b) the board of the company, in the manner contemplated in subsection (3), except to the extent that the Memorandum of Incorporation provides otherwise.'

round robin resolution. Put differently, can a director exercise this power without restraint and without the need to explain the basis of the decision in a justifiable manner?

[20] Section 74 of the Act enables 'a majority of the directors to pass a round robin resolution in order to avoid a formal meeting of directors provided that, if this is to happen 'each director has received notice of the matter to be decided'.[5] The proviso enables directors to make an informed decision on the subject matter contained in the resolution. Mr Stadler, the managing director of Petrotank, decided to invoke the provisions of s 74 of the Act and in the 'notice' he sent to all the directors on 28 March 2014 stated that the problem was that 'more shares are in issue than have been authorised'. The 'matter to be decided' was contained in the proposed resolution the terms of which I have already quoted in full. No reason and in particular no motivation was given for an increase of the authorised shares to 1 000 000. The justification did not rationally extend beyond an increase to 100 000 shares.

[21] The proviso to s 74 requiring notice is to ensure that directors know what is being decided. Our courts have emphasised the importance of giving notice to directors of a meeting so that the participants are aware not only of the existence of a meeting but of the nature of the business.[6] The purpose of the notice is not only to inform directors of the date of the meeting but the reason therefore. There can surely be no difference between the importance of a notice where a board meeting is called in terms of s 73 of the Act and a notice when the provisions of s 74 of the Act are invoked.

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[5] See fn 1 above.

[6] This principle is of long standing see *African Organic Fertilizers and Associated Industries Limited v Premier Fertilizers Ltd* 1948 (3) SA 233 at 240 (N); *Majola Investments (Pty) Ltd v Uitzigt Properties* (Pty) Ltd1961 (4) SA 705 (T) at 710-711.

[22] CDH's directors knew on 28 March 2014 that the round robin resolution upon which the directors were called to vote was contrary to the proclaimed purpose. They also knew that it was contrary to the MOU. Nonetheless on 31 March 2014 they signed the resolution. The egregious conduct on the part of CDH's directors was compounded when, on 4 April 2014, CDH's directors were reminded that the resolution was contrary to the express purpose as contained in the preamble to the resolution. Mr Sontshaka of Amabubesi wrote to Stadler on 4 April 2014 in this connection:

'It should be noted that there is no impediment in terms of the MOI against employing the methods in s 36(2)(a) and (b) and s 36(3). Therefore, the MOI can be amended by any one of the above methods, but only to the extent that it reflects 100 000 (one hundred thousand) authorised shares, which have already been issued, instead of the current 1000 (one thousand) shares. The current resolution requiring that the authorised share be increased to 1000 000 (one million) is incorrect and needs to be amended accordingly.'

Notwithstanding these objections, and significantly employing the services of a firm other than Petrotank's appointed auditors, the majority proceeded to give effect to the resolution by submitting the resolution to the CIPC for filing.

[23] What is surprising is that CDH never sought to explain the reason as to why, in supposedly 'correcting' the patent error in the MOI, its nominees on Petrotank's board resolved to pass a resolution to increase the authorised shares to 1 000 000 rather than 100 000. This clearly called for an explanation on at least the two occasions when Amabubesi's directors questioned the conduct of CDH's directors. The only inference one can draw is that, in passing the resolution contrary to the stated purpose, CDH's nominees on Petrotank's board misrepresented 'the matter to be decided'; ie the purpose they had in mind when introducing the resolution was different from that which appeared in the preamble

and in the email of Stadler of 28 March 2014. They failed to provide any reasons for the actual resolution passed.

[24] These actions of the directors of Petrotank, who were appointed by CDH, amounted to a misrepresentation of the real purpose behind the introduction of the resolution. By their actions and their continued refusal to provide a justification for the need to increase the authorised shares to 1 000 000, they committed a misrepresentation, which at the very least was designed to obfuscate the real purpose behind the resolution. Their conduct did not comport to the standard of good faith required of directors in terms of s 76(3) of the Act[7] and thus raises the question as to whether they exercised their powers as directors for a proper purpose. Directors act beyond their authority when they act in breach of their duty to perform with good faith and in the interests of the company (See M S Blackman 'Directors' Duties to Exercise their Powers for an Authorised Purpose' (1990) 2 *S A Merc LJ* 1 at 6-8).

[25] I accordingly find that the round robin resolution signed on 31 March 2014 was invalid. It follows that the demand for a shareholders meeting to consider a rights issue rested on the unsustainable foundation of this resolution and that there was no basis to compel a shareholders meeting. For these reasons the appeal must fail.

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[7] Section 76(3)*(a)* provides:
'**Standards of directors conduct**
(3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director –
(a) in good faith and for a proper purpose.'

[26] The following order is made:

The appeal is dismissed with costs, such costs to include the costs of two counsel.

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Z Carelse
Acting Judge of Appeal

APPEARANCES:

For Appellant:	BH Swart SC (with him JL Mÿburgh) Instructed by: Horn Attorneys, Johannesburg Honey Attorneys, Bloemfontein
For Respondents:	S Kuny SC (with him T Mamanyuha) Instructed by: Tshisevhe Gwina Ratshimbilani Attorneys, Sandton McIntyre van der Post, Bloemfontein