

COMMERCIAL AND CORPORATE LAW *¹

1 GENERAL

- 1.1 Commerce is regulated by law – common law and legislation - trade custom and usage and legal precedent.
- 1.2 Certain of the more important pieces of legislation in commercial law are – to mention a few – the Companies Act, 61 of 1973 (“Old Act”), the Companies Act, 71 of 2008, Close Corporations Act, 69 of 1984, the Copyright Act, 98 of 1978, the Patents Act, 57 of 1978, the Insolvency Act, 24 of 1936, the Competition Act, 89 of 1998, the Consumer Protection Act, 68 of 2008, the national Credit Act, 34 of 2005, the Labour Relations Act, 66 of 1995, the Electronic Communications and Transactions Act, 25 of 2002, the Constitution of the Republic of South Africa, 108 of 1996 and the King Reports on Corporate Governance.
- 1.3 The new Act has repealed the Old Act, subject to exceptions. Every company registered in terms of the Old Act continues in existence, as if it had been incorporated in terms of the New Act.
- 1.4 Close Corporations may no longer be incorporated under the Close Corporations Act and no company may be converted to a close corporation. Existing close corporations will continue to exist under the Close Corporations Act. A close Corporation may file a notice of conversion into a company, subject to compliance with prescribed requirements, including the filing of a Memorandum of Incorporation (“MOI”).
- 1.5 Individuals primarily drive commerce through recognised and lawful structures, such as a company. These individuals are involved, generally as shareholders and/or directors/management.

2 CORPORATE ENTITIES

- 2.1 It is not required to have a company to conduct business. An individual may conduct business a sole proprietor or group of individuals may conduct business in partnership or through a business trust.
- 2.2 A brief overview follows of the different types of “vehicles” that may be employed to conduct commerce.

*¹ **DISCLAIMER:** this text contains generalisations, is not exhaustive of all the relevant criteria or issues and there may be exceptions to that stated and does not constitute legal advice to the reader. The reader is strongly advised to consult an admitted attorney and not to rely on this text as being sufficient for the reader’s purposes.

Sole Proprietor

- 2.3 Here the individual conducts business in his own name, with or without a trading name, albeit trading names are common place, e.g. John Smith trading as Speed Plumbers.
- 2.4 The individual is subject to all applicable legislation, such as the Value-Added Tax Act, the Labour Relations Act and the like.
- 2.5 Naturally, the individual is liable for all debts of the business, being conducted in his own name.

Partnership

- 2.6 A partnership does not have a legal personality. It is simply a contractual association of persons and has no existence in law independent of its partners.
- 2.7 Although not a company there are ancillary statutory provisions that may apply to a partnership, such as the Consumer Protection Act.
- 2.8 There are no formalities required to establish a partnership, but each partner must make a contribution to the partnership, such as money or labour.
- 2.9 In an ordinary partnership, a partner may contract on behalf of the partnership and so render his co-partners jointly liable. On dissolution of the ordinary partnership each partner is liable fully for all partnership debts, but the partner who pays will have a right of recourse against the other partners for their proportionate share of the debt.
- 2.10 There are also extraordinary partnerships, such as an anonymous partnership and commanditarian partnership (*en commandite* partnership).
- 2.11 In an anonymous partnership, the anonymous partner plays no part in the business and he is not liable to the outside world as partner, but he is liable to his co-partners for his pro-rata share of the partnership debts.
- 2.12 In partnerships *en commandite* – which is similar to an anonymous partnership – the partner *en commandite* contributes a fixed sum, receives a fixed share of the profits, but his liability for partnership debts is limited to his contribution.
- 2.13 The partnership is subject to all applicable legislation, such as the Value-Added Tax Act, the Labour Relations Act and the like.
- 2.14 A partnership may be dissolved by express or tacit agreement between the partners, by operation of law on frustration of the partnership business, on the death of a partner, or the partnership becomes insolvent and any one of the partners renounce the partnership and this will result in its dissolution, but this may lead to liability for damages.
- 2.15 The sequestration of the partnership is governed by the Insolvency Act, which

treats the partnership as an independent entity separate from its members. The partnership estate and the estate of the various ordinary partners are sequestrated simultaneously although separately from the partnership estate.

- 2.16 A partnership contract may be written or oral, but a written partnership agreement is recommended for the sake of avoiding misunderstanding between the partners and for the efficient management of the partnership business.

Business or Trading Trust

- 2.17 A trading trust is a newer type of trust that has recently come into our law with the rise in popularity of the trust as an estate planning tool.
- 2.18 A trading trust provides limited liability protection to the trustees and subsists in perpetuity. This is similar to the benefits offered by a company.
- 2.19 A trading trust is generally not subject to the same strict requirements as a regular trust.
- 2.20 If a trading trust is not operated according to trust law, the trustees face the risk of the trust form being disregarded and the trustees being personally liable for the debts of the trust. However, similar sanctions are provided for in the Companies Act for directors who do not conduct themselves in compliance with the Companies Act.
- 2.21 The trust deed must be in writing and it must be registered in accordance with law. The trust deed must be carefully drafted to ensure that it is legally sound and fit for purpose.

Companies

- 2.22 The Companies Act, 71 of 2008 ("**the Act**") provides for the formation and incorporation of two types of companies, namely profit companies and non-profit companies. The two main types of profit companies are private companies and public companies. The Act repealed the former Companies Act (61), 1973 ("**Old Act**"). Every company incorporated under the Old Act continues to exist.
- 2.23 Under the Act every company will have share capital of no par value. A pre-existing company has share capital at par value but a pre-existing company cannot authorise any new par value shares.
- 2.24 Every company must have a board of directors. The board of directors must manage the business and affairs of the company.
- 2.25 The directors of a company are elected by the shareholders of the company.
- 2.26 A pre-existing company is constituted by its memorandum of association and articles of association, which documents amount to a contract between the company and its shareholders and the shareholders amongst themselves. In terms of the Act, the Memorandum of Incorporation ("**MOI**") in effect, takes the

place of the Memorandum of Association and the Articles of Association. The MOI may deal with anything not addressed by the Act and may alter an alterable provision of the Act.

- 2.27 The existence of the MOI does not preclude shareholders from entering into any agreement with one another concerning any matter relating to the company (commonly referred to as a shareholders agreement), but any such agreement must be consistent with the Act and the company's MOI. Any provision of such an agreement (i.e. shareholders agreement) that is inconsistent with the Act or the company's MOI is void to the extent of the inconsistency. The Old Act did not cater for an MOI and the common practice was for shareholders to regulate their relationship with the company and with each other through the execution of a shareholders agreement. In terms of the Act, the MOI is a fundamental document and there is no need for a separate shareholders agreement, albeit a separate shareholders agreement is not prohibited, subject to the proviso that it does not offend the Act or the MOI. The MOI also deals with the function, rights and duties of directors.
- 2.28 Thus, shareholders should procure that their MOI is carefully drafted.
- 2.29 The MOI must set out the classes of shares and the number of shares that it is authorised to issue and must set out the rights, limitations and other terms of those shares. The MOI can also authorise a stated number of "unclassified" shares which the board of directors can classify.
- 2.30 The two common types of shares are ordinary shares and preference shares. Ordinary shares usually have voting rights but the right to a dividend is not fixed and depends on the discretion of the directors, subject to the MOI. However, ordinary shares can, however, also have a guaranteed or fixed dividend. Preference shares usually have a preference in respect of a dividend that is the declared dividend will be paid first on these shares.
- 2.31 Directors must in the execution of their duties act in compliance with their fiduciary obligations in terms of the common law and as prescribed by the Act. Directors must exercise their powers for the benefit of and in the interests of the company.
- 2.32 The MOI is the most important document in the formation of a company and in the conduct of its affairs and it is the controlling document in the relationship between the company and each shareholder, between the shareholders of the company and between the company and each director. The MOI must therefore be carefully drafted to ensure compliance with the New Act and to protect the interests of shareholders and directors.

3 **UNLAWFUL COMPETITION AND RESTRAINT OF TRADE**

- 3.1 The right to freedom of trade, occupation and profession is entrenched in the Constitution.

- 3.2 The law of competition deals, firstly with those legal rules aimed at the maintenance and promotion of competition and, secondly with those legal rules concerned with the lawfulness of a trader's competitive conduct in relation to his rivals in the market.
- 3.3 The Competition Act, 89 of 1998 is by far the most important factor governing our law of competition.
- 3.4 The doctrine of restraint of trade may affect the enforceability of contracts restricting competition. The two main forms of such contracts concern potential competitors, namely where the seller of the goodwill of a business undertakes not to carry on a similar business in competition with the purchaser and, secondly, where an employee agrees with his or her employer not to compete against the employer. Restraint of trade contracts may also be concluded between existing competitors.
- 3.5 In the circumstances, agreements for the sale of businesses, merges and acquisitions and employment agreements must be carefully drafted to achieve the balance between legal compliance and protecting the interest of each party to the agreement.

4 **DUE DILIGENCE**

- 4.1 Every significant acquisition of a company or a business and a merger and acquisition should be preceded by both a legal and financial due diligence of the entity to be acquired.
- 4.2 A due diligence to verify compliance with all matters legal entails, amongst other things, ensuring that supplier agreements are extant, distributorship agreements are extant, that there is no breach of the applicable agreements or threatened legal action in regard to the breach of an applicable agreement and that all statutory documentation (such as the MOI and shareholders agreement are in existence and in proper form), considering contingent liabilities and subordination agreements.

5 **ARBITRATION AND ALTERNATE DISPUTE RESOLUTION**

- 5.1 Arbitration and alternative dispute resolution mechanisms are an effective means to avoiding and resolving disputes.
- 5.2 This even extends to the scenarios of business restructuring and business rescue.

6 **INSOLVENCY APPLICATIONS AND ENQUIRIES**

- 6.1 It is often necessary to wind-up a debtor who is unable to pay its debts and to interrogate the insolvent debtor's managers and directors to determine the cause of its inability to pay its creditors and if any manager or director may be held personally liable to pay the debts of the insolvent debtor in terms of the Old

Act, the New Act or the common law. This requires invoking the Companies Act as read with the Insolvency Act.

- 6.2 Even in this situation there is often room for mediation and alternative dispute resolution.

7 **CONSTRUCTION AND JOINT VENTURE AGREEMENTS**

- 7.1 Large construction and building projects are mostly preceded by an invitation to tender to execute the works.

- 7.2 The parties to the construction contract are the employer and he employs the building contractor. The intermediate parties are the architect, the engineer and the quantity surveyor.

- 7.3 The contractor's core obligation is the completion and handing over of the building project and that of the employer is the payment of the agreed remuneration. These core obligations are generally housed in a diversity of standard contractual forms or agreements, each with its own characteristics and peculiarities. There are many crucial terms in such contracts not least of which are the terms dealing with variation orders, extra contractual work, timely performance and penalties for failure to perform timely.

- 7.4 It often happens that two contractors join forces to execute a single project. This relationship is generally recorded in a joint venture agreement. The joint venture agreement deals with, amongst other things the roles and responsibilities of each of the parties and the sharing of costs and remuneration.

8 **COMPETITION AND MERGERS**

- 8.1 The right to freedom of trade and to earn a living is entrenched in the Bill of Rights. Competition is comprised of two primary areas, firstly legal rules aimed, in the public interest, at the maintenance and promotion of competition in the economy and the elimination of harmful restrictive trade practices and, secondly, those rules concerned with the lawfulness of a traders competitive conduct in relation to those of his rivals in the economy. In this regard the Competition Act, 89 of 1998 is of great significance.

- 8.2 The Competition Act applies to all economic activity within South Africa and also beyond the borders of South Africa that may have an affect within South Africa.

- 8.3 In the Competition Act a "merger" is defined as the direct or indirect acquisition or establishment of direct or indirect control by one or more firms over the whole or part of the business of another firm. The most common instruments used to achieve a merger are through a purchase or lease of shares, interest, or assets of another firm or the amalgamation or combination with another firm.

- 8.4 The Competition Authorities examine merger activities which could result in an alteration of market structure, particularly that which reduces the level of

competition in the relevant market segment concerned.

9 **COPYRIGHT AND PATENTS**

- 9.1 Intellectual Property (“**IP**”) comprises intangible property that is the result of creativity. IP has a number of sub-categories that are either registerable or unregisterable and all are territorial in nature.
- 9.2 The most common registerable of the IP are patents, trademarks, registered designs and domain names. The most common of the unregisterable IP are copyright, know-how, confidential information and trade secrets.
- 9.3 Copyright is governed by the Copyright Act 98 of 1978. This Act provides that no copyright shall subsist otherwise than by virtue of the Act. The Act does not contain a comprehensive definition of the term “copyright”. However, ownership of the copyright in a work vests, with a few exceptions in its author. In terms of the Patents Act 57 of 1978, provision is made for the registration and granting of patents for inventions. A patent may be granted for any new invention which involves an inventive step and which is capable of being used or applied in trade, industry or agriculture.

10 **E-COMMERCE**

- 10.1 There are two pieces of legislation that are central to e-commerce, namely, The Electronic Communications and Transactions Act, 2000 and the Consumer Protection Act, 2008. These Acts govern Electronic Commerce (including encryption, security and cybercrime) and electronic transactions regarding digital goods and services.
- 10.2 The Constitution guarantees an individual’s right to privacy. This requires that communication by and between individuals not be monitored and intercepted. An important piece of legislation is the Regulation of Interception of Communication and provision of Communication – Related Information Act, 2002 (“**RICA**”). This Act provides that, generally, communications may only be intercepted under guidelines issued by a Judge, but RICA exempts certain types of communications from this restriction, including communication in the workplace where interception and monitoring is necessary for a business purpose or where permission is sought for employees’ communications to be monitored.