COX ATTORNEYS

Simplicity in law

What is meant by an offer to the public in the Companies Act 71 0f 2008.

By

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A private company is famously distinguished from a public company on account of the fact that its memorandum of incorporation must prohibit it from offering its securities to members of the public. This is in terms of section 8(2)(b)(ii)(aa) of the 2008 Companies Act. There is nothing new in this. This restriction has existed in one way or another since the Transvaal Companies Act 31 of 1909 which introduced the private company into our law.

This distinction should not be confused with the much older preoccupation in company law of drawing the line on share dealing between honest albeit foolish endeavour and skulduggery. The latest version of those efforts is to be found in Chapter 4 of the 2008 Companies Act (sections 95 to 111).

There was an anomaly in our law prior to the 2008 Companies Act between what was meant when the term "offer to the public" was used to regulate public share dealing by a company in terms of chapter 6 of the 1973 Companies Act and what was meant when the phrase was used elsewhere in that act to define a private company and when regulating public share dealing by shareholders offered.

This anomaly created unnecessary complications as the test applied in deciding what was an offer of securities to the public by a shareholder in terms of section 142 was different to the one that had to be applied when the company made an offer to the public of its own securities in terms of Chapter 6. The Supreme Court of Appeal when faced with this in Gold Fields Ltd and another v Harmony Gold Mining Company Ltd and others [2005] 3 All SA 114 (SCA) tried to manage the anomaly away. Thus the court ignored the special meaning of an offer to the public defined in chapter 6 of the 1973 Companies Act, relying instead on cases dealing with the general meaning of the term when used in section 141. I refer to the page 117 of the judgement where the Honourable Mr Justice Nugent held.

> *I can add nothing useful to what has been said in earlier cases as to the meaning of "public" (there is no suggestion that the word is used in section 145 in any special sense). In S v V 1977 (2) SA 134 (T) at 137 Franklin J (citing S v Rossouw1 and Tatem Co v Inland Revenue Commissioners2 to similar effect) said that:*
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> *"[t]he ordinary meaning of the word 'public' is the community as a whole rather than the community as an organised body".*
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> *I think it is unhelpful, and potentially misleading, to attempt to determine by inference what is included in an "offer to the public" by referring to the inclusions and exclusions in section 142 (the definition of an "offer to the public") and section 144 respectively, for those inclusions and exclusions might just as well have been inserted to avoid uncertainty. The better approach, in my view, is to ask whether the present offer can properly be said to have been made to the public as that term is ordinarily understood.*

This anomaly no longer exists in the 2008 Companies Act. Section 141 of the 1973 Companies Act which dealt with what are now called secondary offers fell outside Chapter 6 and its definition of an *offer to the public*. Its equivalent under the 2008 Companies Act is section 101 is now part of Chapter 4 and thus subject to the definition of an offer to the public contained in section 95(1)(h). Whatever might be left of the anomaly due to the definition of a private company in section 8(2)(b)(ii)(aa) is disposed of if you treat that requirement mechanically. Thus it's requirement is met merely by the company's memorandum of incorporation containing a provision that states that it must not offer it securities to the public as this is prohibited.

That leaves the much more difficult question of what is meant by an offer to the public in Chapter 4. It is clear that the term still embraces its ordinary meaning. Section 95(1)(h) defines a an offer to the public in these terms:

h) offer to the public"

i) <u>includes</u> an offer of securities to be issued by a company to any section of the public, whether selected—

(aa) as holders of that company's securities;

(bb) as clients of the person issuing the prospectus;

(cc) as the holders of any particular class of property; or

(dd) in any other manner; but

ii) does not include—

(aa) an offer made in any of the circumstances contemplated in section 96; or

(bb) a secondary offer effected through an exchange.

I think the intention is clear. The definition of an offer to the public must be applied literally as defined. The term no longer has an ordinary meaning separate and distinct from the definition quoted above. That definition of course includes the ordinary meaning of the term but this cannot be separated from the defined meaning as the Supreme Court of Appeal did in the Goldfields case. This is because the anomaly the court relied on in that case no longer exists. The definition of an offer to the public must be strictly applied to Chapter 4.

The harsh consequences that would result from this literal application of the section is ameliorated by the change to the definition of the word "offer" in section 95(1) (g). The scope of what is generally referred to as an offer to the public no longer includes an invitation to make an offer for securities in a company. The definition now reads:

"offer", in relation to securities, means an offer made in any way by any person with respect to the acquisition, for consideration, of any securities in a company.

Thus companies both public and private or their shareholders who invite members of the public to make offers for their securities will not be affected Chapter 4. However I must sound a note of caution here. This should not be seen as an open invitation for companies or shareholders evade Chapter 4 by hawking their shares to the public under the smokescreen of an invitation to make an offer. Apart from the anti avoidance measures contained in section 6 , section 5(1) requires the 2008 Companies Act to be interpreted having regard to the purposes set out in section 8. Schemes designed to defeat or evade Chapter 4 are likely to fall foul of these sections. The ordinary meaning of an offer to the public will continue to apply. Such schemes will in my opinion be treated as offers to the public as defined in section 95(1)(h).

I think the approach adopted by the Honourable Mr Justice Wallis in Financial Services Board v Dynamic Wealth Ltd and others [2012] 1 All SA 135 (SCA) may be indicative of the approach that will be adopted in this regard. In that matter Dynamic Wealth Limited argued that its investment scheme was not a collective investment scheme as defined in Collective Investment Schemes Control Act of 2002 because its members were a restricted circle of individuals engaged in a domestic or private

business venture and thus fell outside the definition of members of the public. That argument was summarily dismissed in these terms:

> *This claim was shown to be false when lists of the participants were provided to the inspectors. By way of example, a tennis association; a primary school and a school for the blind; a church; an optometrist and other businesses; several trusts, both family and charitable; some deceased estates and a number of individuals from various parts of the country and having little other than their investment in that portfolio in common. The answering affidavit said that membership was restricted to persons invited to join through Dynamic Wealth's network of independent financial advisers. However, this network was 470 strong and it recruited literally thousands of investors who invested hundreds of millions of Rand through these associations. There can be no doubt that investments were being solicited from members of the public.*

It may be an oversimplification but for practical intents and purposes I think one could do a lot worse that apply the so called duck test in these cases. So:

> *if it looks like a duck, swims like a duck, and quacks like a duck, then it probably is a duck.*

After all, as the Honourable Mr Justice Nicholas observed in S v. Rossouw [1971] 3 All SA 135 T, the question what constitutes an offer to the public is one that can only be answered with reference to the circumstances of the particular case. A similar approach has been adopted in other countries.

This may not be ideal given that it is a criminal offence to make an offer of securities to the public in contravention of Chapter 4. However I suggest this is a lot better than trying to lay down hard and fast rules for a problem made uniquely fluid by the infinite possibilities that arise when human ingenuity and optimism grapple with the prospect of making a profit.

So in summary, I suggest:

1. A private company is such inter alia because its memorandum of incorporation must prohibit it from offering its securities to members of the public. As such it cannot raise funds by offering its shares to the public in the manner contemplated in Chapter 4
2. This prohibition does not extend to shareholders of private companies who like their counterparts in public companies, may offer those shares to the public provided they comply with section 101.
3. Courts may not longer ignore the definition of an offer to the public contained in section 95(1)(h) of the 2008 Companies Act as they did under the 1973 Companies Act. An offer to the public as defined in that section must be strictly applied to Chapter 4 of the 2008 Companies Act.
4. An offer to the public does not include an invitation to the public to make an offer for shares unless that invitation is in substance, albeit not in form, an offer to the public.

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