

# The Device of Weighted Votes in Blocking the Removal of Directors from Office under the South African Companies Act 71 of 2008

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## Abstract

A director may serve a company in more than one capacity. In his capacity as a shareholder, a director may hold voting rights in the company. One consideration regarding the removal of a director from office is their removal by shareholders in circumstances where the directors are themselves shareholders in the company and hold weighted votes. This article appraises whether, under the South African Companies Act 71 of 2008, a shareholding-director who holds shares with weighted votes would validly and lawfully be able to block his removal from office by the company's shareholders. This article makes suggestions regarding the use of weighted votes to block the removal of directors from office, and calls for an important amendment to the South African Companies Act 71 of 2008 to prevent weighted votes being used as a device to block the removal of directors from office.

## Keywords

Weighted votes, loaded voting rights, removal of directors, shareholding-directors, blocking of votes, entrenching directors in office

## INTRODUCTION

Under the South African Companies Act 71 of 2008 (South African Companies Act), which came into force on 1 May 2011, directors may be removed from office by either the shareholders or the company's board of directors. Previously, under section 220 of the South African Companies Act 61 of 1973, only the shareholders had been statutorily empowered to remove a director from the board.<sup>1</sup> This provision has been retained in the new South African Companies Act in the form of section 71(1), which empowers a

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1 On sec 220 of the South African Companies Act 61 of 1973, see *Stewart v Schwab* 1956 (4) SA 791 (T); *Swerdlow v Cohen and Others* 1977 (3) SA 1050 (T); *Amoils v Fuel Transport (Pty) Ltd* 1978 (4) SA 343 (W); *Barlows Manufacturing Co Ltd and Others v RN Barrie (Pty) Ltd and Others* 1990 (4) SA 608 (C); and *James North (Zimbabwe) (Pvt) Ltd v Mattinson* 1990 (2) SA 229 (ZHC).

company's shareholders to remove a director from office by an ordinary resolution.<sup>2</sup> With regard to the removal of directors by the board of directors, section 71(3) of the new South African Companies Act now permits the board of directors to remove a director from office in instances where (i) a company has more than two directors and (ii) a shareholder or director alleges that a director of the company has become ineligible or disqualified to be a director, or has become incapacitated to the extent that the director is unable to perform the functions of a director and is unlikely to regain that capacity within a reasonable time, or has neglected or been derelict in the performance of the functions of a director.<sup>3</sup>

It is imperative that shareholders have the power to remove directors from office, in order to make directors accountable to shareholders and to give directors a strong inducement to serve the shareholders' interests.<sup>4</sup> In light of the effects of the separation of ownership and control<sup>5</sup> in a company,

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2 Sec 71(1) states: "Despite anything to the contrary in a company's Memorandum of Incorporation or rules, or any agreement between a company and a director, or between any shareholders and a director, a director may be removed by an ordinary resolution adopted at a shareholders meeting by the persons entitled to exercise voting rights in an election of that director, subject to subsection (2)." Sec 71(2) sets out the procedures that must be followed before the shareholders may consider such a resolution.

3 Under sec 71(3), the board of directors, other than the director concerned, must determine the matter by resolution, and may remove a director whom it has determined to be ineligible or disqualified, incapacitated, or negligent or derelict, as the case may be.

4 RG Bailey "Shareholder control over management: The removal of directors" (1974) 20 *McGill Law Journal* 85 at 86; LA Bechuk "The myth of the shareholder franchise" (2007) *Virginia Law Review* 675 at 680.

5 In many small private companies the directors and the shareholders are the same persons. In larger companies though, as famously documented by Berle and Means in their landmark study in 1932 (AA Berle and GC Means *The Modern Corporation & Private Property* (1947, The Macmillan Company)), ownership and control of companies do not vest in the same persons. The effect of the split in ownership and control is that a large body of shareholders has been created who exercise virtually no control over the wealth that they have contributed to the enterprise, while the ownership interest held by the controlling group, being the directors, is only a very small fraction of the total ownership of the company. A detailed discussion of the separation of ownership and control is beyond the scope of this article, but see further: GR Sullivan "The relationship between the board of directors and the general meeting in limited companies" (1977) 93 *Law Quarterly Review* 569 at 579; EF Fama and MC Jensen "Separation of ownership and control" (1983) 26/2 *The Journal of Law and Economics* 301 at 301; AR Pinto "Corporate governance: Monitoring the board of directors in American corporations" (1998) 46 *The American Journal of Comparative Law* 317; J Hill "Visions and revisions of the shareholder" (2000) 48 *American Journal of Comparative Law* 39 at 39; SM Bainbridge *Corporate Law* (2nd ed, 2009, Thomson Reuters Foundation Press) at 72–75; B Steyn and L Stainbank "Separation of ownership and control in South African-listed companies" (2013) 16/3 *South African Journal of Economic and Management Sciences* 316 at 316; RP Austin and IM Ramsay *Ford, Austin and Ramsay's Principles of Corporations Law* (16th ed, 2015, LexisNexis Butterworths) at 238; D French, S Mayson and C Ryan *Mayson, French & Ryan on Company Law* (32nd ed, 2015, Oxford University Press) at 433–34; and B Hannigan *Company Law* (4th ed, 2016, Oxford University Press) at 183–86.

particularly in large companies, the power conferred on shareholders to remove directors from office strikes a balance between the attenuated power of control conferred on shareholders with the power of directors to manage the company.<sup>6</sup> Shareholders' power to remove directors from office is also important in light of the fact that the South African Companies Act has, for the first time in South African corporate law history, conferred on the board of directors a statutory power to manage the business and affairs of the company.<sup>7</sup> Such power is now original and is no longer required to be delegated to the board by the shareholders through the company's constitution. The shareholders' power to remove directors is thus a critical tool in the hands of shareholders, a form of corporate democracy, and a necessary and key provision of modern company law.<sup>8</sup> As the Supreme Court of Delaware asserted in *Unocal Corp v Mesa Petroleum Co*, "[i]f the stockholders are displeased with the action of their elected representatives, the powers of corporate democracy are at their disposal to turn the board out".<sup>9</sup> In *Aronson v Lewis* the same court similarly asserted that a stockholder is not powerless to challenge director action that results in harm to the corporation and that the machinery of corporate democracy is a potent tool to redress the conduct of a "torpid or unfaithful management".<sup>10</sup>

When a director is involved with a company in more than one capacity, such as where the director is also an employee or a shareholder, the relationship between the director and the company becomes complicated. Before a director is removed from office, cognisance must be taken of any other capacities in which the director serves the company, so that the consequences may be considered before the director is removed from office. In his capacity as a shareholder, a director may hold voting rights in the company. A director who is also a shareholder with voting rights is, in his capacity as a shareholder, entitled to vote on the resolution proposed for his own removal as a director.<sup>11</sup> The threshold for passing a shareholders' resolution to remove a director from office is more than 50 per cent of the voting rights exercised on the resolution.<sup>12</sup> This threshold may not be increased in a company's

6 BJ Cartoon "The removal of company directors" (1980) *The Journal of Business Law* 17 at 17.

7 South African Companies Act, sec 66(1) empowers the board of directors of a company to manage the company's business and affairs, save to the extent that the act or the company's memorandum of incorporation provides otherwise. See further *Kaimowitz v Delahunt and Others* 2017 (3) SA 201 (WCC), paras 12–13.

8 Cartoon "The removal of company directors", above at note 6.

9 493 A.2d 946 (Del 1985) at 959.

10 473 A.2d 805 (1984) at 811.

11 R Cassim "Governance and the board of directors" in FHI Cassim (ed) *Contemporary Company Law* (2nd ed, 2012, Juta) 400 at 445.

12 Under the South African Companies Act, sec 71(1), a director may be removed by an ordinary resolution adopted at a shareholders' meeting by the persons entitled to exercise voting rights in an election of that director. Sec 1 defines an "ordinary resolution" as meaning a resolution adopted with the support of more than 50% of the voting rights exercised on the resolution, or a higher percentage as contemplated in sec 65(8).

memorandum of incorporation.<sup>13</sup> It follows that a director who holds more than 50 per cent of the voting rights in a company would always be empowered to prevent his own removal from office by voting against the ordinary resolution in his capacity as a shareholder.

Another important consideration regarding the removal of a director from the company concerns the removal of directors from office by shareholders in circumstances where the directors are themselves shareholders in the company and hold weighted votes or loaded voting rights in the company. This article appraises whether, under the South African Companies Act, a shareholding-director who holds shares with weighted votes or loaded voting rights would validly and lawfully be able to block his removal from office by the company's shareholders. This article contends that weighted votes should not be accepted in South African company law as a valid method to block the removal of directors under the South African Companies Act. It calls for an amendment to the South African Companies Act to prevent weighted votes being used as a device to evade the right of shareholders to remove directors from office.

A notable provision of the South African Companies Act is section 5(2), which provides that, to the extent appropriate, a court interpreting or applying the South African Companies Act may consider foreign law. In *Nedbank Ltd v Bestvest 153 (Pty) Ltd*; *Essa and Another v Bestvest 153 (Pty) Ltd and Others* the High Court, per Gamble J, remarked that company law in South Africa has for many decades tracked the English system and has taken its lead from the relevant English Companies Act and jurisprudence.<sup>14</sup> For this reason, this article critically evaluates the controversial and leading English case of *Bushell v Faith*<sup>15</sup> and appraises its applicability to South African company law. Judge Gamble observed further that section 5(2) of the South African Companies Act now encourages South African courts to look further afield and to have regard in appropriate circumstances to other corporate law jurisdictions, be they American, European, Asian or African, in interpreting the South African Companies Act. Accordingly, where applicable, this article also refers to the legal position on weighted votes in other comparable jurisdictions.

## THE MEANING OF "WEIGHTED VOTES" OR "LOADED VOTING RIGHTS"

The expression "weighted votes" or "loaded voting rights" (used interchangeably in this article) is used to describe the device by which certain shares are

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13 See *id.*, sec 65(8), which explicitly prohibits a company's memorandum of incorporation from increasing the threshold to pass an ordinary resolution for the removal of a director under sec 71.

14 2012 (5) SA 497 (WCC), para 26.

15 [1970] AC 1099 (HL).

given additional voting strength above that enjoyed by other shares that, in every other respect, are identical to their participation in the company.<sup>16</sup> In essence, weighted votes or loaded voting rights are voting rights that are disproportionate to shareholdings.<sup>17</sup> Weighted votes are often used to protect minority shareholders.<sup>18</sup> Through the use of weighted votes, persons with relatively small financial contributions to a company may have a relatively large voting power conferred on them.<sup>19</sup>

Weighted votes or loaded voting rights may apply generally to all resolutions or may be confined to resolutions on specific matters.<sup>20</sup> Weighted votes would be exercisable when voting takes place on a poll, not when voting takes place on a show of hands. Under section 63(5) of the South African Companies Act, if voting is by a show of hands, a shareholder or their proxy has one vote, irrespective of the number of voting rights that person would otherwise be entitled to exercise. If, on the other hand, voting on a particular matter is by polling, a shareholder or their proxy has the number of votes determined in accordance with the voting rights associated with the securities held by that shareholder.<sup>21</sup>

According to section 37(2) of the South African Companies Act, each issued share of a company, regardless of its class, has one general voting right associated with it,<sup>22</sup> except to the extent provided otherwise by (i) the act or (ii) the preferences, rights, limitations and other terms determined by the company's memorandum of incorporation in accordance with section 36 of the act. It follows that a company's memorandum of incorporation may depart from the default rule of each share having one general voting right.

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16 “‘Weighted’ or ‘loaded’ votes in private companies” (1977) *The South African Company Law Journal* D5 at D5.

17 FHI Cassim “The division and balance of power between the board of directors and the shareholders: The removal of directors” (2013) 29/1 *Banking and Finance Law Review* 151 at 164. See further on loaded voting rights: D Kershaw *Company Law in Context: Text and Materials* (2nd ed, 2012, Oxford University Press) at 713; French, Mayson and Ryan Mayson, *French & Ryan on Company Law*, above at note 5 at 95–96; PL Davies and S Worthington *Gower Principles of Modern Company Law* (10th ed, 2016, Sweet & Maxwell) at 380; and Hannigan *Company Law*, above at note 5 at 96–97.

18 “‘Weighted’ or ‘loaded’ votes”, above at note 16.

19 *Model Business Corporation Act with Official Comments and Reporter's Annotations* (vol 2, 4th ed, 2013, American Bar Association) at 7-115.

20 “‘Weighted’ or ‘loaded’ votes”, above at note 16.

21 South African Companies Act, sec 63(6). Under sec 63(7) a polled vote must be held on a particular matter if a demand for such a vote is made by at least five persons having the right to vote on that matter, or by a person or persons who together are entitled to exercise at least 10% of the voting rights entitled to be voted on that matter.

22 Id, sec 1 defines a “voting right” as meaning, with respect to any matter to be decided by a company, the rights of any holder of the company's securities to vote in connection with that matter (in the case of a profit-company) or the rights of a member to vote in connection with the matter (in the case of a non-profit company). “Voting power” constitutes the voting rights that may be exercised by a particular person in connection with a matter to be decided by a company, as a percentage of all such voting rights: *ibid*.

Under section 36(1)(b) of the South African Companies Act, a company's memorandum of incorporation must set out, with respect to each class of shares, the preferences, rights, limitations and other terms associated with that class, subject to section 36(1)(d) of the act. Under section 36(1)(d), a company's memorandum of incorporation may set out a class of shares: (i) without specifying the associated preferences, rights, limitations or other terms of that class; (ii) for which the board of directors must determine the associated preferences, rights, limitations or other terms; and (iii) that must not be issued until the board has determined the associated preferences, rights, limitations or other terms. These provisions authorize the board of directors to determine the preferences, rights, limitations and other terms of a particular class of shares. A further notable provision of the act is section 37(5)(a), which permits a company's memorandum of incorporation, subject to any other law, to establish for any particular class of shares, preferences, rights, limitations or other terms that confer special, conditional or limited voting rights. Sections 36(1), 37(2) and 37(5)(a) therefore authorize a company's memorandum of incorporation to confer more than one voting right on some classes of shares. Thus, under the South African Companies Act it is possible for a shareholding-director to have loaded votes and for additional voting rights to be attached to certain shares held by him.

The approach adopted to loaded voting rights under the South African Companies Act is consistent with that adopted in the United States of America (USA) under the Revised Model Business Corporation Act 1984. Section 7.21(a) of this act states that each share is entitled to one vote unless otherwise provided in the articles of incorporation. Thus companies may depart from the default rule of giving each share one vote by appropriate provisions in their articles of incorporation. Likewise, the default rule in Delaware, under section 212(a) of the Delaware General Corporation Law, is that each share has one vote. Companies in Delaware may however opt out of this rule by inserting appropriate provisions in the certificate of incorporation.<sup>23</sup>

Loaded voting rights are also permissible under section 250E(1) of the Australian Corporations Act of 2001.<sup>24</sup> In *Amalgamated Pest Control Pty Ltd and Another v McCarron and Others* the Supreme Court of Queensland held that it is permissible for a company's constitution to confer a voting right or voting privilege that is disproportionate to the size of the member's shareholding.<sup>25</sup> This case concerned the validity of a provision in the plaintiff's

23 The Delaware General Corporation Law, sec 212(a) states: "Unless otherwise provided in the certificate of incorporation ... each stockholder shall be entitled to 1 vote for each share of capital stock held by such stockholder."

24 This section provides that, subject to any rights or restrictions attached to any class of shares, at a meeting of members of a company with a share capital, on a show of hands each member has one vote, and on a poll each member has one vote for each share they hold. It follows that a particular class of shares may have specific rights attached to it, such as loaded voting rights.

25 (1994) 13 ACSR 42 at 45–46.

articles of association. Article 27D provided that, at any general meeting, the permanent governing director was entitled to a weighted vote equivalent to 26 per cent of the total votes available, whether or not he was a member of the company. The Supreme Court of Queensland held that article 27D was valid save for the part that permitted a weighted vote “whether or not” the governing director was a member.<sup>26</sup> The court severed this part of article 27D and held that, provided that it is associated with membership, a voting privilege unrelated to the size of the shareholding of the member was valid.<sup>27</sup> The court thus recognized the freedom given to shareholders to contract with each other, in accordance with the company’s constitution, to determine their respective rights and responsibilities.<sup>28</sup> The only limit expressed by the court on this right is that the articles of association must provide that the individual in question is a shareholder of the company.<sup>29</sup>

Section 284 of the Companies Act of 2006 of the United Kingdom (UK) (UK Companies Act of 2006) confers on a shareholder one vote on a resolution on a show of hands and one vote in respect of each share where voting takes place on a poll, but permits a company’s articles of association to alter shareholders’ voting rights.<sup>30</sup> Accordingly, in the UK loaded voting rights are also permissible if the articles of association so provide.

Under the South African Companies Act, loaded voting rights are permissible with regard to both public and private companies. In contrast, under section 195(1) of the Companies Act 61 of 1973, public companies were not permitted to issue shares with loaded voting rights: only private companies were permitted to do so. The new South African Companies Act does not distinguish between the types of company that may make provision for loaded voting rights in their memorandum of incorporation. While public companies are entitled to issue shares with loaded voting rights, public companies listed on the Johannesburg Stock Exchange (JSE) are prohibited from doing so. Paragraph 3.29 of the JSE Listings Requirements provides that securities in each class for which listing is applied must rank *pari passu* in respect of all rights. According to paragraph 3.29(c) of the JSE Listings Requirements, this means that the securities must carry the same rights as to unrestricted transfer, attendance and voting at general and annual general meetings and in all other respects. Paragraph 4.18 of the JSE Listings Requirements states that the JSE will not grant a listing to a company with low or high voting securities or allow an existing listed company to issue low or high voting securities. A low voting security is one that confers on its holder reduced voting rights in

26 *Id* at 45.

27 *Id* at 45–46.

28 S Armstrong “Australia: Company law: Weighted voting rights” (1995) 6/5 *International Company and Commercial Law Review* 96 at 97.

29 *Ibid*.

30 See the UK Companies Act of 2006, sec 284(4), which provides that the provisions of sec 284 are subject to any provision of the company’s articles of association.

comparison with the voting rights conferred on the holders of equity securities already listed by the issuer.<sup>31</sup> A high voting security is one that confers on its holder enhanced voting rights in comparison with the voting rights conferred on the holders of equity securities already listed by the issuer.<sup>32</sup>

Listed companies in Australia are also prevented from issuing shares with loaded voting rights. ASX Listing Rule 6.8 provides that, on a resolution to be decided on a show of hands, each holder of an ordinary security or a preference security who has a right to vote must be entitled to one vote. ASX Listing Rule 6.9 provides that, on a resolution to be decided on a poll, each holder of an ordinary security or a preference security who has a right to vote must be entitled to one vote for each fully paid security and a fraction of a vote for each partly paid security.<sup>33</sup>

The same approach has been adopted in the UK, which recently tightened its listing principles and requirements to prevent listed companies from issuing shares with loaded voting rights. Premium Listing Principle 3 of Listing Rule 7.2.1A contained in chapter 7 of the UK Listing Rules requires equity shares admitted to a premium listing to carry an equal number of votes on any shareholder vote.<sup>34</sup> A premium listing is only available to equity shares issued by trading companies or closed or open-ended investment entities, and means that the company is expected to meet the UK's highest standards of regulation and corporate governance.<sup>35</sup>

In contrast, in the USA, some exchanges, such as the New York Stock Exchange (NYSE), permit new applicants to list with weighted voting structures.<sup>36</sup> The rules of the NYSE do not however permit an issuer, once listed, to implement a weighted voting rights structure that would prejudice the interests of the company's existing shareholders.<sup>37</sup> Likewise, the Hong Kong Stock Exchange recently introduced new rules to permit new listing applicants to adopt weighted voting structures.<sup>38</sup> The voting power attached to weighted voting shares must however be capped at not more than ten times the voting

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31 JSE Listings Requirements, para 4.19.

32 *Id.*, para 4.20.

33 The ASX Listing Rules are enforceable against listed entities under the Australian Corporations Act of 2001 (see secs 793C and 1101B).

34 This rule came into force on 16 May 2014. The UK Listing Rules are a set of regulations that apply to a company listed on a UK stock exchange and are subject to the oversight of the UK Listing Authority.

35 The distinction between a standard listing and a premium listing was introduced in the UK in 2010. While the shares listed with a standard listing must comply with the minimum standards, shares listed with a premium listing must comply with more onerous standards.

36 See NYSE Listed Company Manual, sec 313.00(A) (voting rights policy).

37 *Id.*, sec 313.00(A).

38 On 24 April 2018 the Stock Exchange of Hong Kong Limited announced that a new chap 8A on weighted voting rights would be inserted into the Listing Rules of the Stock Exchange of Hong Kong Limited. The rules took effect on 30 April 2018.



power of ordinary shares.<sup>39</sup> These new rules were implemented after a four year debate in Hong Kong as to whether the exchange should permit new listing applicants to adopt weighted voting structures after the decision by certain high-profile technology companies to list in the USA instead of in Hong Kong.<sup>40</sup>

## THE CONFERRAL OF LOADED VOTING RIGHTS ON DIRECTORS IN THEIR CAPACITY AS DIRECTORS

In South Africa, unless a company's memorandum of incorporation provides otherwise, each director has one vote on a matter before the board.<sup>41</sup> It follows that a director may have more than one vote on a matter before the board of directors if this is specifically stated in a company's memorandum of incorporation. For instance, the memorandum of incorporation may provide that the chairman of the board will have two votes on any resolution to remove a fellow board member from office.

It is important to note that loaded voting rights that are conferred on a director in his capacity as a director do not confer any power for him to influence a proposed resolution to remove him from office. Section 71(3) of the South African Companies Act explicitly states that the board "other than the director concerned" must determine the matter of the director's removal by resolution. Thus a director who is the subject of a removal resolution may not, in his capacity as a director, vote on his own removal from office. This is logical, because a director who is the subject of a removal resolution would naturally be inclined to vote against his own removal. It follows that a provision in a company's memorandum of incorporation that confers loaded votes on a director in his capacity as a director with regard to a proposed resolution

39 Id, rule 8A.10. Refer further to id, chap 8A for the other conditions and safeguards regulating weighted voting rights in companies listed on that stock exchange. For example: the weighted voting structure must be share based (rule 8A.07); shareholders with non-weighted voting rights must be entitled to cast at least 10% of the votes that are eligible to be cast on resolutions at the listed issuer's general meetings (rule 8A.09); issuers with weighted voting rights will be required to include the warning, "A company controlled through weighted voting rights" on the front page of all corporate documents (rule 8A.37); and issuers with weighted voting rights will be required to describe in their listing documents and periodic financial reports, circulars, notifications and announcements their weighted voting rights structure, the rationale for having a weighted voting rights structure and the associated risks for shareholders (rule 8A.37).

40 J Griffiths and C McKenzie "Hong Kong Stock Exchange brings in landmark changes to allow weighted voting rights shares" (27 April 2018) *Asia Pacific Law Alert*, available at: <<https://www.nixonpeabody.com/-/media/Files/Alerts/2018-April/HK-Stock-Exchange-weighted-voting-right%20structures.ashx>> (last accessed 1 May 2019); Hong Kong Exchanges and Clearing Limited "Concept paper: Weighted voting rights" (August 2014) at 7-9, available at: <<http://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2011-to-2015/August-2014-Weighted-Voting-Rights/Consultation-paper/cp2014082.pdf>> (last accessed 1 May 2019).

41 South African Companies Act, sec 73(5)(c).

to remove him from office would be void<sup>42</sup> and that such loaded votes would not be exercisable by the director.

The capacity in which a director is voting on a proposed removal resolution is important. The issue of a director holding loaded voting rights in his capacity as a shareholder would only arise when the shareholders purport to remove him from office and not when the board of directors purports to remove him from office. However, the board must take cognisance of whether a shareholding-director holds loaded voting rights in his capacity as a shareholder since this may present an obstacle to the shareholders removing the director (as discussed below). In such event, provided there are valid grounds to do so, the board of directors would have to take the necessary steps to remove the shareholding-director from office under section 71(3) of the South African Companies Act.

In small private companies where the directors may also be shareholders, it is particularly important to be aware of the capacity in which a director is voting on a proposed removal resolution. Errors in the voting capacity of the directors may easily be made in such companies. For example, such an error occurred in the USA decision of *Iwasaki v Iwasaki Bros Inc*,<sup>43</sup> where a director in a small private family-owned company was removed from the board of directors by a three-to-two vote of the board, rather than by a vote of the shareholders. All of the directors were also shareholders. Two of the directors voting for the removal held two-thirds of the company's shares. The director in question had the right to vote on his own removal in his capacity as a shareholder, but had abstained from voting. Although it was improper for the board to vote on the removal resolution since it was contrary to the applicable statute, the Oregon Court of Appeals nevertheless did not invalidate the removal of the director from office on the ground that the outcome of the vote would have been the same if the vote had been exercised at a shareholders' meeting.<sup>44</sup> Under the South African Companies Act it would be improper and invalid for a director to vote on a board resolution to remove him from office, since this is expressly prohibited by section 71(3) of the act. For this reason it is important to be mindful of the capacity in which directors who are also shareholders vote on removal resolutions.

## THE REMOVAL OF SHAREHOLDING-DIRECTORS WITH LOADED VOTING RIGHTS

The important question that arises is whether a director who holds loaded voting shares in a company would validly be able to use his loaded voting rights

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42 See *id.*, sec 15(1)(a) and (b), essentially providing that each provision in a company's memorandum of incorporation must be consistent with the Companies Act and is void to the extent that it contravenes, or is inconsistent with, the Companies Act.

43 Or App 649 P.2d 598.

44 *Id.* at 601.

to defeat a shareholders' resolution to remove him from office as a director. This question was the crux of the controversial landmark English case of *Bushell v Faith*.<sup>45</sup>

### ***Bushell v Faith***

In *Bushell v Faith* the company had an issued share capital of 300 shares. The shares were divided equally between the appellant Mrs Bushell, her sister Dr Bayne and their brother, the respondent, Mr Faith. Each shareholder held 100 shares. Mrs Bushell and Mr Faith were the company's sole directors. Article 9 of the articles of the company, which was a small private company, stated: "[i]n the event of a resolution being proposed at any general meeting of the company for the removal from office of any director, *any shares held by that director shall on a poll in respect of such resolution carry the right to three votes per share* and regulation 62 of Part 1 of Table A shall be construed accordingly."<sup>46</sup>

The two sisters were unhappy with their brother's conduct as a director and purported to remove him from office. On a show of hands the resolution was successfully passed because the two sisters voted in favour of the resolution. Faith demanded that voting take place on a poll. On a poll, both sisters voted in favour of the removal of Faith, while Faith voted, in his capacity as a shareholder, against the purported resolution to remove him from office. A dispute arose as to whether or not the resolution had been passed. Bushell contended that the resolution had been passed by 200 votes to 100. Faith argued that, in accordance with article 9 of the company's articles of association, his 100 shares carried 300 votes, and that the resolution had therefore been defeated by 300 votes to 200. The question before the court was whether article 9 was valid and applicable, or whether it was to be treated as overridden by section 184 of the UK Companies Act of 1948 (the equivalent of section 168 of the UK Companies Act of 2006)<sup>47</sup> and therefore void. Section 184 of the UK Companies Act of 1948 enabled a company to remove a director, by ordinary resolution, before the expiry of his period of office "notwithstanding anything in the articles".

The court *quo* found in favour of Bushell, on the basis that article 9 of the company's articles of association was invalid because it infringed section 184 (1) of the UK Companies Act of 1948. Ungoed-Thomas J expressed the view that it would "make a mockery of the law" to uphold article 9 of the company's

45 Above at note 15.

46 Emphasis added. Table A, part 1, reg 62 provided: "Subject to any rights or restrictions for the time being attached to any class or classes of shares, on a show of hands every member present in person shall have one vote, and on a poll every member shall have one vote for each share of which he is the holder."

47 The UK Companies Act of 2006, sec 168(1) provides that a director of a company may be removed at any time by an ordinary resolution of shareholders, despite anything contained in any agreement between the director and the company.

constitution.<sup>48</sup> Faith appealed and the Court of Appeal unanimously reversed the decision of the court a quo. In finding in favour of Faith, the Court of Appeal was of the view that the object of section 184 was to increase the powers of the shareholders in general meeting by providing that “nothing higher than a simple majority of votes was required”<sup>49</sup> to remove a director from office. The Court of Appeal remarked further that section 184 did “nothing to restrict a company’s ability to allocate voting rights to shares in varying degrees and circumstances”.<sup>50</sup> On a further appeal, by Bushell, the House of Lords, by a majority of four to one, upheld the Court of Appeal decision and found in favour of Faith.

The House of Lords held that article 9 was valid and enforceable, and that it was not in conflict with section 184(1) of the UK Companies Act of 1948 since that act did not prevent special voting rights being attached to special circumstances and particular types of resolutions.<sup>51</sup> The court found that the practice of loaded voting rights was valid and recognized and that Parliament had not sought to fetter a company’s right to issue shares with such loaded voting rights<sup>52</sup> but had, instead, left to companies the “liberty to allocate voting rights as they pleased”.<sup>53</sup>

With regard to the words “notwithstanding anything in its articles” contained in section 184(1), Lord Upjohn of the House of Lords remarked that the reason why Parliament had included these words was to ensure that a director would be removable by virtue of an ordinary resolution instead of an extraordinary resolution<sup>54</sup> (that is, by a 75 per cent majority). The Court of Appeal in *Bushell v Faith and Another*<sup>55</sup> also found that the words “notwithstanding anything in its articles” in section 184(1) simply ensured that a requirement for a greater majority than a simple majority for passing the removal resolution, would be of no effect.

Lord Reid in the House of Lords accepted that the extra voting power conferred by article 9 of the company’s articles of association on a director whose removal is proposed would make it impossible for any resolution for the removal to be passed if that director voted against the resolution.<sup>56</sup> The learned judge admitted that article 9 was “obviously designed”<sup>57</sup> to evade

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48 This decision of Ungoed-Thomas J, dated 3 December 1968, does not appear to have been reported. This quote is taken from the judgment of Harman LJ in the decision of the UK Court of Appeal in *Bushell v Faith and Another* [1969] 1 All ER 1002 at 1004 and from the judgment of Lord Upjohn in the House of Lords in *Bushell v Faith*, above at note 15 at 1107–08.

49 *Bushell v Faith and Another*, id at 1003, per Harman LJ.

50 Id at 1006, per Russell LJ.

51 *Bushell v Faith*, above at note 15 at 1109, per Lord Upjohn.

52 Ibid.

53 Id at 1110, per Lord Donovan.

54 Id at 1108.

55 Above at note 48 at 1104, per Russell LJ.

56 *Bushell v Faith*, above at note 15 at 1105, per Lord Reid.

57 Ibid.

section 184(1) of the UK Companies Act of 1948. Despite the admission that article 9 was designed to make the director irremovable, Lord Reid agreed with the majority decision of the House of Lords that article 9 was valid. It appears though that he had difficulty with his decision, because he commented that his agreement with the majority decision was “with some reluctance”.<sup>58</sup>

The minority judgment in *Bushell v Faith*, per Lord Morris of Borth-y-Gest, the sole dissident, accepted that some shares may carry a greater voting power than others, but proclaimed that this does not warrant a “device”<sup>59</sup> such as that introduced by article 9 of the articles of association. The learned judge held that the “unconcealed effect” of article 9 was “to make a director irremovable”.<sup>60</sup> He stated further:

“If the question is posed whether the shares of the respondent possess any added voting weight the answer must be that they possess none whatsoever beyond, if valid, an ad hoc weight for the special purpose of circumventing section 184. If article 9 were writ large it would set out that a director is not to be removed against his will and that in order to achieve this and to thwart the express provision of section 184 the voting power of any director threatened with removal is to be deemed to be greater than it actually is. The learned judge<sup>61</sup> thought that to sanction this would be to make a mockery of the law. I think so also.”<sup>62</sup>

### Evaluation of *Bushell v Faith*

The majority judgment in *Bushell v Faith* adopted a literal and narrow approach to interpreting article 9 and section 184(1) of the UK Companies Act of 1948,<sup>63</sup> rather than a purposive approach. The House of Lords interpreted section 184(1) strictly, according to the words of the section as enacted by Parliament. *Bushell v Faith* remains a controversial decision, and commentators have been divided on the merit and validity of the judgment, with some expounding the correctness of the decision and others strongly criticizing it.

In defence of the majority judgment in *Bushell v Faith*, Cartoon contends that, if the company’s shareholders had specifically, deliberately and intentionally included in the company’s constitution a provision with the effect of excluding the benefits of section 184 of the UK Companies Act of 1948, they had only themselves to blame when Faith exercised his three votes

58 Ibid.

59 Id at 1106.

60 Ibid.

61 Lord Morris of Borth-y-Gest was referring here to the judgment of the court a quo, per Ungood-Thomas J, which had found in favour of Bushell.

62 *Bushell v Faith*, above at note 15 at 1106.

63 See *Muir v Lampl and Another* [2005] 1 HKLRD 338 at 345; E Boros “Virtual shareholder meetings: Who decides how companies make decisions?” (2004) 28 *Melbourne University Law Review* 265 at 283; and A Dignam *Hicks & Goo’s Cases and Materials on Company Law* (7th ed, 2011, Oxford University Press) at 334.

against the removal resolution, so defeating it.<sup>64</sup> Beuthin supports the Court of Appeal decision<sup>65</sup> and remarks that it may be desirable for directors to be safeguarded in directorships by means of special voting rights.<sup>66</sup> Hahlo assumes that the Court of Appeal decision in *Bushell v Faith and Another* is good law and accepts that it is possible to give a shareholder or group of shareholders multiple voting rights on a resolution for the removal of a director with the consequence that the removal of a director may be prevented.<sup>67</sup>

In *Muir v Lampl*<sup>68</sup> the High Court of Hong Kong accepted that the majority judgment in *Bushell v Faith* was correct. The court distinguished between an unqualified provision that prohibits the shareholders from removing a particular person as a director and one that confers weighted voting rights on a shareholder. The court asserted that the first type of agreement constitutes an unlawful fetter on the statutory power conferred by section 157B of the Companies Ordinance (cap 32) (the equivalent provision to section 71(1) of the South African Companies Act).<sup>69</sup> The court commented that, bearing in mind the background leading to the enactment of section 157B of the Companies Ordinance and its equivalent provision in the UK, these statutory provisions are intended to be strong provisions safeguarding shareholders' residual indirect control in the management of the company.<sup>70</sup> It observed further that these provisions provide an important underpinning for the checks and balances in the distribution of power between the shareholders and directors.<sup>71</sup> For these reasons the court questioned whether absolute immunity from removal could ever be justified.<sup>72</sup> The court did, however, assert that there is a conceptual difference between weighted voting rights and an absolute agreement prohibiting the removal of a director.<sup>73</sup> In the former case, the court stated that the result of the vote is dictated by the vote cast by the shareholder with weighted votes, whereas in the latter the result is dictated by the terms of the shareholders' agreement prohibiting the removal

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64 Cartoon "The removal of company directors", above at note 6 at 19–20.

65 Above at note 48.

66 RC Beuthin "A director firmly in the saddle" (1969) 86 *South African Law Journal* 489 at 489.

67 HR Hahlo "Restrictions on the alteration of articles" (1969) 86 *South African Law Journal* 349 at 351.

68 Above at note 63.

69 Id at 346, per Lam J. The Companies Ordinance (cap 32), sec 157(B) provided: "A company may by ordinary resolution remove a director before the expiration of his period of office, notwithstanding anything in its memorandum or articles or in any agreement between it and him: Provided that this subsection shall not, in the case of a private company, authorize the removal of a director holding office for life on the commencement of the Companies (Amendment) Ordinance 1984 (6 of 1984)."

70 *Muir v Lampl*, *ibid*.

71 Id at 347.

72 *Ibid*.

73 *Ibid*.

of a director and is more acute and direct.<sup>74</sup> Based on this reasoning, the court accepted that the weighted voting rights could be exercised in a manner that would result in the defeat of a shareholders' resolution to remove a director.<sup>75</sup>

Lord Donovan of the House of Lords justified the decision of the majority judgment in *Bushell v Faith* by stating that article 9 was needed to protect shareholders who were directors in small companies. He reasoned that provisions such as article 9 were a safeguard against family quarrels having their repercussions in the boardroom of small family companies running a family business.<sup>76</sup> In light of this rationalization of the majority judgment, Davies and Worthington suggest that the decision of the majority judgment may be justified in small private companies, which are in effect an incorporated partnership or a quasi-partnership, where it is not unreasonable for each "partner" to be entitled (as under partnership law) to participate in the management of the firm in the absence of his agreement to the contrary and to protect himself against removal by his fellow partners.<sup>77</sup> Rutabanzibwa argues that weighted voting rights are in fact useful in protecting the interests in small private companies that are established on the basis of mutual confidence and trust.<sup>78</sup> Birds et al<sup>79</sup> also express the view that the ratio of *Bushell v Faith* may be legitimate in the context of small private companies. On the basis of this reasoning and justification it is arguable that the ratio of *Bushell v Faith* must be confined to private companies and that it does not apply to public companies.<sup>80</sup>

On the other hand, other commentators have argued that the decision in *Bushell v Faith* runs contrary to the spirit of section 184(1) of the UK

74 Ibid.

75 Id at 344 and 347.

76 *Bushell v Faith*, above at note 15 at 1110–11.

77 Davies and Worthington *Gower Principles of Modern Company Law*, above at note 17 at 380. A quasi-partnership usually involves a small private company, which in effect runs as a partnership between the shareholders. The shareholders agree to go into a business venture together on the basis of an agreement or understanding that all the shareholders will participate in the management of the company's business and that they will all be appointed as directors of the company. See *Ebrahimi v Westbourne Galleries Ltd and Others* [1972] 2 All ER 492 (HL) at 500; *Barnard v Carl Greaves Brokers (Pty) Ltd and Others and Two Other Cases* 2008 (3) SA 663 (C), para 11; *Croly v Good and Others* [2010] EWHC 1 (Ch), paras 9 and 89–93; *De Sousa and Another v Technology Corporate Management (Prop) Ltd and Others* 2017 (5) SA 577 (GJ), para 47; PG Fitzpatrick "Re Westbourne Galleries Ltd" (1971) 22/1 *Northern Ireland Legal Quarterly* 60 at 60; Kershaw *Company Law in Context*, above at note 17 at 674–79; and French, Mayson and Ryan *Mayson, French & Ryan on Company Law*, above at note 5 at 71.

78 AP Rutabanzibwa "What is golden in the golden share? Company law implications of privatisation" (1996) 17/2 *Company Lawyer* 40 at 43.

79 J Birds et al *Boyle and Birds' Company Law* (9th ed, 2014, Jordan Publishing) at 563.

80 See further D Botha "Some aspects concerning the removal of directors" (1973) *De Rebus Procuratoriis* 465 at 467; A Keay "Company directors behaving poorly: Disciplinary options for shareholders" (2007) *Journal of Business Law* 656 at 672–73; Kershaw *Company Law in Context*, above at note 17 at 227; and French, Mayson and Ryan *Mayson, French & Ryan on Company Law*, above at note 5 at 446.

Companies Act of 1948. Article 9 of the company's articles in effect enabled a director of the company to prevent a resolution being passed for his removal from office since he could out-vote the other two shareholders.<sup>81</sup> This meant that directors of the company were effectively entrenched in office.<sup>82</sup> Collier remarks that the minority judgment of Lord Morris of Borth-y-Gest is more in consonance with the spirit and intention of the law.<sup>83</sup> Schmitthoff also opines that the decision of the House of Lords "contravenes the spirit, if not the letter, of section 184"<sup>84</sup> and remarks further that the House of Lords decision will go down in legal history as one of the most remarkable instances of judicial interpretation defeating the clear intention of the legislator.<sup>85</sup> Prentice expresses the view that the decision of the Court of Appeal, affirmed by the House of Lords, "reduced section 184 to an empty rhetorical gesture".<sup>86</sup> Kaye remarks that the majority judgment of the House of Lords in *Bushell v Faith* sanctioned a scheme that succeeds in making "a mockery of the law".<sup>87</sup> Griffin agrees with the minority judgment that the acceptance of a weighted voting clause made a mockery of the law because it nullifies the existence of the statutory power to remove a director.<sup>88</sup>

In *Swerdlow v Cohen and Others* Botha J expressed the view that the majority decision in *Bushell v Faith* was incorrect.<sup>89</sup> He agreed with the minority judgment by Lord Morris of Borth-y-Gest, which he stated was "unanswerable".<sup>90</sup> This view is however only an obiter dictum, because the facts in *Swerdlow v Cohen* are distinguishable from those in *Bushell v Faith*. In *Swerdlow v Cohen* the directors had a right to veto a resolution. While in a sense the power to veto a resolution may be regarded as a special voting right, it is not a species of a loaded or weighted voting right that must be taken into account in

81 Cassim "The division and balance of power", above at note 17 at 164.

82 Ibid.

83 JG Collier "Company - Power to remove director by ordinary resolution - Weighted voting - Whether ordinary resolution" (1970) 28 *The Cambridge Law Journal* 41 at 42.

84 CM Schmitthoff "House of Lords sanctions evasion of Companies Act" (1970) *The Journal of Business Law* 1 at 2.

85 Id at 1.

86 DA Prentice "Removal of directors from office" (1969) 32 *Modern Law Review* 693 at 696.

87 RG Kaye "A mockery of the law?" (1970-71) 2 *Kingston Law Review* 63 at 66.

88 S Griffin *Company Law Fundamental Principles* (4th ed, 2006, Pearson / Longman) at 288. For further discussion of *Bushell v Faith*, see Botha "Some aspects concerning the removal of directors", above at note 80 at 467; "Weighted' or 'loaded'", above at note 16; "Weighted' votes again" (1977) *The South African Company Law Journal* D17; Rutabanzibwa "What is golden in the golden share?", above at note 78 at 42-43; Boros "Virtual shareholder meetings", above at note 63 at 282-84; Cassim "The division and balance of power", above at note 17 at 164-65; Kershaw *Company Law in Context*, above at note 17 at 223-28; Birds et al *Boyle and Birds' Company Law*, above at note 79 at 562-63; French, Mayson and Ryan *Mayson, French & Ryan on Company Law*, above at note 5 at 95-96 and 446; Davies and Worthington *Gower Principles of Modern Company Law*, above at note 17 at 380; and Hannigan *Company Law*, above at note 5 at 174.

89 1977 (1) SA 178 (W) at 184-85.

90 Ibid.



counting the votes in order to determine whether an ordinary resolution has been passed.<sup>91</sup> Botha J held that the power of veto was invalid when invoked to defeat a resolution to remove certain directors under section 220 of the Companies Act 61 of 1973.<sup>92</sup> On appeal, Margo J confirmed the dictum of Botha J in the court a quo, but found that it was unnecessary to examine the validity of the decision in *Bushell v Faith* or to express an opinion on the main issue in *Bushell v Faith*, on the basis that the facts in the case before him were distinguishable from those in *Bushell v Faith*.

### The application of *Bushell v Faith* in South African law

It is an open question whether the majority judgment of *Bushell v Faith* would be followed by a South African court. There is no difference in general principle between the UK law that applied in *Bushell v Faith* with regard to loaded voting rights and section 37(2) of the new South African Companies Act, which permits loaded voting rights to be conferred on shareholders. As indicated above, section 5(2) of the South African Companies Act permits a court to consider foreign law whenever appropriate. On this basis, the dictum of the majority judgment of *Bushell v Faith* would have persuasive authority in South African law.

A further reason why *Bushell v Faith* would have persuasive authority in South African law is that section 71(1) of the South African Companies Act contains similar wording to that used in section 184(1) of the UK Companies Act of 1948. Section 71(1) states that a director may be removed from office “[d]espite anything to the contrary in a company’s Memorandum of Incorporation or rules, or any agreement between a company and a director, or between any shareholders and a director”. As discussed above, with regard to the words “notwithstanding anything in its articles” contained in section 184(1) of the UK Companies Act of 1948, the House of Lords asserted that the reason why Parliament had included these words was to ensure that a director would be removable by virtue of an ordinary resolution instead of an extraordinary resolution.<sup>93</sup> The Court of Appeal in *Bushell v Faith and Another* also found that the words “notwithstanding anything in its articles” in section 184(1) ensured that a requirement for a greater majority than a simple majority for passing the removal resolution would be of no effect.<sup>94</sup>

The UK Companies Act of 2006 did not undo the effect of *Bushell v Faith*.<sup>95</sup> The majority judgment is still applicable in the UK, save for listed

91 Id at 188.

92 Id at 188–89.

93 *Bushell v Faith*, above at note 15 at 1108.

94 Above at note 48 at 1004.

95 See Griffin *Company Law Fundamental Principles*, above at note 88 at 288; Keay “Company directors behaving poorly”, above at note 80 at 672–73; Birds et al *Boyle and Birds’ Company Law*, above at note 79 at 563; and Hannigan *Company Law*, above at note 5 at 174.

companies.<sup>96</sup> This means that loaded voting rights remain a valid method of entrenchment for directors in the UK, and a court will enforce loaded voting rights conferred on a shareholding-director even if the loaded voting rights are exercised in a manner that thwarts a shareholders' resolution to remove a director. Griffin asserts that the continued acceptance and validity of weighted voting clauses in the UK is indicative of the view that statutory powers, while workable in theory, can in specified circumstances be manipulated to such an extent that they are of little practical worth.<sup>97</sup>

Section 168 of the UK Companies Act of 2006 states that a company may by ordinary resolution at a meeting remove a director before the expiry of his period of office "notwithstanding anything in any agreement between it and him", deviating from the wording of its predecessor, section 184(1) of the UK Companies Act of 1948, which stated "notwithstanding anything in its articles". In light of this change in wording, Dignam remarks that *Bushell v Faith* is no longer of direct authority in the UK in this area of the law.<sup>98</sup> It is however submitted, with respect, that, since the House of Lords in *Bushell v Faith* found that the words "notwithstanding anything in its articles" in section 184(1) of the UK Companies Act of 1948 did no more than ensure that a director is removable by an ordinary resolution instead of by a special resolution and that these words did not prevent loaded voting rights being used to prevent the removal of a shareholding-director, the omission of these words from section 168(1) of the UK Companies Act of 2006 would not alter the effect of *Bushell v Faith* on the removal of directors by loaded voting rights. Section 303 of the UK Companies Act of 1985, the predecessor to section 168 of the UK Companies Act of 2006, stated that a company may by ordinary resolution remove a director before the expiry of his period in office "notwithstanding anything in its articles or in any agreement between it and him". The deletion of the reference to the "articles" may suggest that the removal right no longer explicitly overrides a contrary intention in the articles of association. This interpretation is however incorrect. The UK government remarked that the reason why the reference to the "articles" in section 168 of the UK Companies Act of 2006 was deleted was that it was not necessary to state expressly that the provisions of the UK Companies Act of 2006 would have effect notwithstanding anything in the company's articles since, in any case, "the articles may not override the requirements set out in the Bill" (now the UK Companies Act of 2006).<sup>99</sup>

96 As discussed above, listed companies in the UK may not issue shares with loaded voting rights.

97 Griffin *Company Law Fundamental Principles*, above at note 88 at 288.

98 Dignam *Hicks & Goo's Cases and Materials*, above at note 63 at 334.

99 *Hansard* May 2006, vol 681, part 142 at column 826, per Lord Sainsbury of Turville. See further: Kershaw *Company Law in Context: Text and Materials*, above at note 17 at 223; and S Worthington *Sealy & Worthington's Text, Cases and Materials in Company Law* (11th ed, 2016, Oxford University Press) at 300.

While *Bushell v Faith* may have persuasive authority in South African law, it is submitted that the House of Lords adopted a limited interpretation of the words “notwithstanding anything in its articles” in section 184(1) of the UK Companies Act of 1948. The wide wording of section 184(1) indicates that the section was aimed at preventing *any* form of entrenchment of directors by whatever means possible.<sup>100</sup> In a similar vein it is arguable that giving the words “despite anything to the contrary” in section 71(1) of the South African Companies Act their ordinary meaning indicates that the legislature intended to override *any* method, whether direct or indirect, designed to ensure that a director is not removed from office,<sup>101</sup> and not just to ensure that a director is removed from office by an ordinary resolution. Accordingly, if an article in a company’s memorandum of incorporation confers loaded voting rights on a particular class of shares, which has the effect of enabling an ordinary resolution to remove a director to be defeated, it is submitted that such an article would be an indirect method of entrenching a director in office and that it would be in breach of section 71(1).

A critical provision of the South African Companies Act is the anti-avoidance provision contained in section 6(1). This provision must be considered in evaluating the weight of the majority judgment in *Bushell v Faith* in South African law. This provision empowers a court, on application by the South African Companies and Intellectual Property Commission, the Takeover Regulation Panel or an exchange in respect of a company listed on an exchange, to declare any agreement, transaction, arrangement, resolution or provision of a company’s memorandum of incorporation or rules: “(a) to be primarily or substantially intended to defeat or reduce the effect of a prohibition or requirement established by or in terms of an unalterable provision of this Act; and (b) void to the extent that it defeats or reduces the effect of a prohibition or requirement established by or in terms of an unalterable provision of this Act”.

A court would have to examine the substance of a provision to ascertain whether it is primarily or substantially intended to circumvent an unalterable provision in the South African Companies Act.<sup>102</sup> In the absence of judicial authority, it is arguable that the test for “primarily” would probably be subjective. On the other hand, the phrase “substantially intended to defeat or reduce the effect of” arguably implies that the objective effect of the provision must be examined. It is consequently arguable that, if the primary intention of a provision in the memorandum of incorporation is not to defeat the effect of a prohibition or requirement established by or under the South African Companies Act but objectively it has this effect, the provision could nevertheless contravene section 6(1) of the act.<sup>103</sup>

100 Kaye “A mockery of the law?”, above at note 87 at 65.

101 Cassim *Contemporary Company Law*, above at note 11 at 448.

102 FHI Cassim “Introduction to the new Companies Act” in *id.*, 1 at 7.

103 For discussion of the substance over form approach and for illustrative purposes in tax law, where anti-avoidance provisions are well-established in South African law, refer to

The South African Companies Act contains two main types of provision. The first is the unalterable provision. An unalterable provision is a provision that does not expressly contemplate that its effect on any particular company may be negated, restricted, limited, qualified, extended or otherwise altered in substance or effect by a company's memorandum of incorporation or rules.<sup>104</sup> A company may not "contract out" of the unalterable provisions of the South African Companies Act.<sup>105</sup> A company's memorandum of incorporation may however impose a more onerous requirement on the company than that contained in an unalterable provision of the act.<sup>106</sup> The second type of provision is the alterable provision, which is a provision of the South African Companies Act in which it is expressly contemplated that its effect on a particular company may be negated, restricted, limited, qualified, extended or otherwise altered in substance or effect by that company's memorandum of incorporation.<sup>107</sup> Most of the alterable provisions of the South African Companies Act are "opt out" provisions, that is, they will apply to a company unless it opts out of them by expressly stipulating so in its memorandum of incorporation, as opposed to the "opt in" provisions that do not apply to a company unless it specifically so provides in its memorandum of incorporation.<sup>108</sup>

It is submitted that the power conferred by section 71(1) of the South African Companies Act on the shareholders to remove directors is an unalterable provision as it does not expressly contemplate that its effect may be negated, restricted, limited, qualified, extended or otherwise altered in substance or effect by a company's memorandum of incorporation. It follows that no company memorandum of incorporation may negate, restrict, limit, qualify, extend or alter the substance or effect of the power conferred by section 71(1) on the shareholders to remove directors. It is arguable that, if a company's memorandum of incorporation contains a provision conferring loaded voting rights on certain shares with the intention of defeating a resolution to remove a director from office, that provision may be declared void under

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*Commissioner for Inland Revenue v Conhage (Pty) Ltd (formerly Tycon (Pty) Ltd)* 1999 (4) SA 1149 (SCA); *Commissioner for the South African Revenue Service v NWK Ltd* 2011 (2) SA 67 (SCA); and *Sasol Oil v CSARS* (923/2017) [2018] ZASCA 153 (9 November 2018).

104 South African Companies Act, sec 1.

105 See "Memorandum on the objects of the Companies Bill, 2008" in the Companies Bill [B 61D-2008] para 5.

106 See South African Companies Act, sec 15(2)(a)(iii), which provides that a company's memorandum of incorporation may impose on the company a higher standard, greater restriction, longer period of time or any similarly more onerous requirement than would otherwise apply to the company in terms of an unalterable provision of the act.

107 Ibid. These types of provisions usually have the introductory phrase "unless prohibited by its memorandum of incorporation" or "except to the extent that the memorandum of incorporation of a company provides otherwise".

108 MF Cassim "Formation of companies and the company constitution" in Cassim (ed) *Contemporary Company Law*, above at note 11, 105 at 126.

section 6(1) of the South African Companies Act on the basis that it is primarily intended to defeat section 71(1).<sup>109</sup> It is submitted that, if a provision in the memorandum of incorporation were to confer loaded voting rights on shareholders with regard to voting generally on ordinary resolutions, and not specifically with regard to voting on an ordinary resolution to remove a director, but the substantial effect of the exercise of the loaded voting rights on a removal resolution is that the effect of section 71(1) is defeated, that provision would also fall foul of section 6(1). A loaded voting rights clause that has the practical effect of thwarting the removal of a director would clearly defeat the intention behind section 71(1) and render the statutory provision of little practical worth. It is accordingly submitted that, under the South African Companies Act, a provision in the memorandum of incorporation conferring loaded voting rights may be declared void under section 6(1) to the extent that it defeats section 71(1).

It is noteworthy that the legislature stated in section 65(8) of the South African Companies Act that, while the threshold for passing an ordinary resolution may be increased, this may not be done with regard to an ordinary resolution for the removal of a director. Presumably the legislature enacted this restriction in order to prevent a company, in its memorandum of incorporation, from increasing the threshold to pass an ordinary resolution with the intention of making it difficult or impossible to remove a director from office. It is submitted that, since loaded voting rights may have the effect of making it difficult or impossible to remove a shareholding-director from office, in light of section 6(1) of the act, a similar exception should be carved out in section 37(2) to the effect that a company may not permit a share to carry more than one vote where this will have the effect of defeating section 71(1). It is accordingly submitted that the South African legislature must tighten section 37(2) in order to prevent an evasion of section 71(1) by the device of loading of voting rights. The author therefore proposes the following amendment to section 37(2) of the South African Companies Act:

- “(2) Each issued share of a company, regardless of its class, has associated with it one general voting right, except to the extent provided otherwise by -
- (a) this Act; or
  - (b) the preferences, rights, limitations and other terms determined by or in terms of the company’s Memorandum of Incorporation in accordance with section 36,
- provided that the Memorandum of Incorporation may not make provision for an issued share of a company to have associated with it more than one general voting right in circumstances where this will have the effect of primarily or substantially defeating section 71(1) of this Act.”<sup>110</sup>*

109 Cassim “The division and balance of power”, above at note 17 at 165.

110 The recommended changes are shown in italics.

## CONCLUSION

This article has discussed the removal of a director from office in circumstances where the director in question is a shareholder of the company and holds loaded voting rights in the company. It has discussed and evaluated the controversial and landmark English case of *Bushell v Faith*,<sup>111</sup> in which a shareholding-director successfully prevented his removal from office by exercising his loaded voting rights. It has argued that there is no difference in general principle between the UK law that applied in *Bushell v Faith* with regard to loaded voting rights and section 37(2) of the South African Companies Act, which permits loaded voting rights to be conferred on shareholders. It is submitted that, while the majority decision in *Bushell v Faith* may have persuasive authority in South African law, a provision in a company's memorandum of incorporation that confers loaded voting rights on a particular class of shares and has the effect of defeating an ordinary resolution to remove a director, would be an indirect method of entrenching a director in office. It is further submitted that such a provision may contravene section 71(1) of the South African Companies Act, and may also fall foul of the anti-avoidance provision in section 6(1) of the act.

The South African legislature must tighten section 37(2) of the South African Companies Act, which permits loaded voting rights to be issued, in order to prevent an evasion of section 71(1) of the act by the loading of voting rights. Shareholders' power to remove directors is a form of corporate democracy and is a necessary and key provision of modern company law. The author proposes an amendment to section 37(2), to the effect that a company may not permit shares to have more than one vote per share where this would have the effect of primarily or substantially defeating section 71(1) of the act.

Until South African courts authoritatively decide on the impact of the ratio of *Bushell v Faith* on South African law or the legislature clarifies the legal position in this regard, it remains an open question whether *Bushell v Faith* would be followed in South African law and whether loaded voting rights attaching to a director's shares may be used as a device to defeat a shareholders' resolution for his removal. Both public and private companies (but not listed companies) must carefully consider whether their memoranda of incorporation permit loaded voting rights to be exercised by a shareholding-director and whether the shareholding-director would effectively be able to use his loaded voting rights to block his removal from office.

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111 Above at note 15.