AANTEKENINGE

COMPANY RULES

OPSOMMING

Maatskappyreëls

Die praktyk was dat organe van 'n maatskappy ingelyf ingevolge die Maatskappywet 61 van 1973 die bevoegdheid gegee is om reëls te maak. Hierdie praktyk was ook van toepassing op maatskappye anders as artikel 21-maatskappye wat as huiseienaarsverenigings gefunksioneer het. Die rede vir sodanige bevoegdheidsverlening was gewoonlik dat sulke reëls makliker gewysig kon word as die destydse akte of statute van die maatskappy of as 'n aandeelhouersooreenkoms. Die Maatskappywet 71 van 2008 ("2008 Maatskappywet") maak nou in artikel 15 voorsiening vir die maak, wysiging of herroeping van sulke reëls, ook vir maatskappye anders as maatskappye sonder winsbejag, die opvolger van die artikel 21-maatskappy. Die direksie het nou die bevoegdheid om reëls te maak tensy dit uitgesluit word in die akte van oprigting. Hierdie reëls moet voldoen aan die vereistes van artikel 15(3) en 15(4), maar die direksie moet ook hulle vertrouenspligte, soos vervat in artikel 76(3) van 2008 Maatskappywet, nakom as sodanige reëls gemaak, gewysig of herroep word. Die reëls moet deur 'n meerderheidsbesluit bekragtig word en die meerderheid moet hulle bevoegdheid op so 'n wyse uitoefen dat dit aan die vereistes van die gemenereg en die 2008 Maatskappywet voldoen. Alhoewel reëls dus oënskynlik makliker gemaak, gewysig of herroep kan word, moet daar nou aan verskillende vereistes op verskillende vlakke in die maatskappy voldoen word vir die reëls om geldig te wees.

1 General

Companies under the Companies Act 61 of 1973 ("1973 Companies Act") in many instances gave the power to make "rules" to organs of the company, very often to the board of directors (see Cilliers *et al Cilliers and Benade Corporate law* (2000) 84 in respect of organs of a company). The reason for conferring this power was, usually, because the only alternative to regulating certain relationships such as that between the shareholders/members and the company, would have been to amend the contractual relationship, that is, of the shareholder/member, which would have entailed as a minimum first step, the amendment of the then memorandum of association and/or the articles of association with the prescribed majority or, if applicable, amending a shareholders' agreement with unanimous consent. This practice of conferring a power to make rules to an organ of the company was usually in respect of home owners' associations where a person who acquired property within a particular residential estate would also have become or would have been deemed to become a member of a then section 21 company in terms of the 1973 Companies Act (see, as one example, *Abraham v Mount Edgecombe Country Club Estate Management Association Two (RF) (NPC)* [2014] JOL 32322 (KZD) paras 2 5). The same practice was transferred to and is also implemented in terms of the Companies Act 71 of 2008 ("2008 Companies Act"/"Act") with the home owners' association now

being a non-profit company ("NPC") as regulated by, *inter alia*, section 10 and schedule 1 of the Act. Item 4(2)(b) of schedule 1 of the 2008 Act, however, now prohibits a practice under the 1973 Companies Act whereby a person acquiring property would have been deemed to become a member of the section 21 company (now the NPC). This obviously will affect the use of the NPC and especially the terms of the contract for the acquisition of property, but is not the main issue in this discussion. In section 1 of the 2008 Companies Act, a "shareholder" is defined as the holder of a share and who is entered in the certificated securities register held under section 50 (or in the uncertificated securities register as held by a participant or by the central securities depository (s 52 of the 2008 Companies Act and chapter IV of the Financial Markets Act 19 of 2012). A "share" is defined in section 1 as a share in a profit company. A NPC, not being a profit company, does not have shareholders, but "members" (s 1 of the 2008 Companies Act and also s 10(4) that provides that in respect of a NPC with voting members, a reference in the 2008 Companies Act to "shareholders" or 'holders of securities" will also refer to "members": see also Delport (ed) *Henochsberg on the Companies Act 71 of 2008* (2011) (Service Issue 14) (hereafter *Henochsberg*) 52(1F)–52(1G)).

The power to make rules has also been, and still is, conferred on certain corporate entities by legislation. An example is the body corporate of sectional title schemes in terms of section 10(2)(a) of the Sectional Titles Schemes Management Act 8 of 2011 (see GN 1231 in *GG* 40335 of 7 October 2016). The rules in terms of the latter Act for these corporate entities are not regulated by or in terms of the Companies Act, as these entities do not fall within the definition of "company" in terms of section 1 of the 2008 Companies Act. However, the power to make rules for companies as defined in section 1 of the 2008 Companies Act is now not only expressly recognised, but also regulated in terms of that Act. This now applies to all companies and is not only restricted to the hitherto practice only in respect of the NPC. In this note, the power to make rules as conferred in the 2008 Companies Act is discussed, especially with reference to case law. Special attention is given to the legal basis of the power, the limits to this power, the process that needs to be followed, as well as the requirements in terms of the general (not only corporate) common law and the 2008 Companies Act.

2 Rules in terms of the Companies Act

2 1 Power to make rules

Section 15 of the 2008 Companies Act regulates the power to make rules and provides as follows:

> "(3) Except to the extent that a company's Memorandum of Incorporation provides otherwise, the board of the company may make, amend or repeal any necessary or incidental rules relating to the governance of the company in respect of matters that are not addressed in this Act or the Memorandum of Incorporation, by –
>
> (a) publishing a copy of those rules, in any manner required or permitted by the Memorandum of Incorporation, or the rules of the company; and
>
> (b) filing a copy of those rules."

The 2008 Companies Act provides for alterable and unalterable provisions in the memorandum of incorporation (see s 15(2); Cassim *et al Contemporary company law* (2011) 123; *Henochsberg* 71; Stoop "Alterable and unalterable provisions of the Companies Act 71 of 2008: Recent cases expose inherent uncertainties" 2016 (1) *J of Corporate and Commercial L & Practice* 40–51). However, the provisions

regarding rules are default provisions, such as the *naturalia* of a contract (see Van Huyssteen *et al Contract general principles* (2016) para 9.136), unless excluded by the memorandum of incorporation. The provisions in respect of the rules also cannot be amended by the memorandum of incorporation as the wording of the section, such as the use of the word "must", makes it clear that all the requirements apply. In this sense, therefore, it would be unalterable.

Section 15(4) provides that a rule contemplated in section 15(3) must be consistent with the 2008 Companies Act and the company's memorandum of incorporation, and any such rule that is inconsistent with the Act or the company's memorandum of incorporation is void to the extent of the inconsistency. The logical process therefore to determine the integrity/validity of the rule itself, is to determine whether it is consistent with the 2008 Companies Act and the company's memorandum of incorporation. In respect of the latter, an "internal" enquiry will also be necessary. This is the case because the provisions of the company's memorandum of incorporation must likewise not be in contravention of the Act, and will be void to the extent that they are in such contravention (s 15(1)(b)) of the Act). Therefore, if the particular provision in the memorandum of incorporation is void due to inconsistency with the Act, a rule inconsistent with this "void" provision may be otherwise valid. If the memorandum of incorporation contains a particular provision, such as proxy requirements in section 58, a rule cannot regulate that position differently. If that is the case, the rule will be void. However, as the next step, the exercise of the power to make the rules must comply with section 15(3) that requires that the rules must be "necessary" or "incidental" relating to the governance of the company. A rule that is not in contravention of a provision in the memorandum of incorporation, therefore, theoretically at least, can still pertain to that provision. The requirement, however, is that if the board, who has the power to make, amend or repeal these rules, acts as such, but the rules are not necessary or incidental to the governance of the company, even if consistent with the Act and the company's memorandum of incorporation, these rules will be *ultra vires* the power given to the board and should therefore be void *ab initio*. The first question here, therefore, is what is meant with "governance". If this is determined, the next question will be whether that rule is necessary for or incidental to governance.

The word "governance" defies an exact and exhaustive definition, and it also depends in which context it is used. It is susceptible to various different meanings. It is submitted that "governance" in this context, also based on the legal obligations that the rules create, should be interpreted to mean the internal operations and relations and the powers and rights and obligations of the board, the board and other committees and the shareholders in respect of the company, to the exclusion of third parties (see also the reference to "governance" in Part E of Chapter 3 of the Act) and that "corporate governance" would refer to the effect of these operations and powers in respect of outside stakeholders (see, eg, *King IV Report on corporate governance for South Africa* (2016); *South African Broadcasting Corporation Ltd v Mpofu* [2009] 4 All SA 169 (GSJ); *Mthimunye-Bakoro v Petroleum Oil and Gas Corporation of South Africa (SOC) Limited* [2015] JOL 33744; Naidoo *Corporate governance – An essential guide for South African companies* (2017); Du Plessis *et al Principles of contemporary corporate governance* (2015) 1–3; *Henochsberg* 51–52 and authorities cited in Esser and Delport "Shareholder protection in terms of the Companies Act 71 of 2008" 2016 *THRHR* 1–29).

Certain relationships then, by definition, would fall outside "governance" as defined above and rules purported to be made or amended in respect of these relationship should be *ultra vires* the powers of the board. This would include rules that are purported to exclusively regulate the relationship as between shareholders, such as pre-emption rights between those shareholders or alternative dispute resolution in the event of disputes between shareholders. As such, it would not be necessary to enquire whether those rules were necessary or incidental to the governance of the company, as the critical first requirement that it must be in respect of governance is not complied with.

The basis of the "governance", need not, however, be the rules. It can be the memorandum of incorporation and, it is submitted, also the Act. In such a case, the rules must be necessary or incidental to the governance provision and cannot purport to amend the governance provision. In *Venter v Silver Lakes Homeowners Association NPC* (444994/2016) [2017] ZAGPPHC 11 (20 January 2017), the first of the "proxy cases" that culminated in *Barry v Clearwater Estates NPC* 2017 3 SA 364 (SCA), the rule of the homeowners' association (NPC company) provided that a member may be represented by proxy at general meetings, provided that a person, other than the chairperson of the general meeting, may not act as proxy for more than five members, unless he holds direct or indirect ownership of these members' units exceeding five units. The court found (paras 13.2 13.2 13.4) that if this was incorporated in the memorandum of incorporation, it would have been void as it is in conflict with the provisions of section 58 of the Act that provides that a shareholder/member can appoint any individual at any time to act as proxy. A limitation in respect of the appointment of a particular individual, being someone that already holds five proxies, therefore is in conflict with the "any individual" in section 58, with the result that it is void. The same principles also apply to rules as is provided in section 15(4), and the purported rule therefore is void. However, the court remarked that section 15(3) of the 2008 Companies Act states that

> "except to the extent that a company's MOI (memorandum of incorporation) provides otherwise, the board of the company may make, amend or repeal any necessary or incidental rules relating to the governance of the company in respect of matters that are not addressed in the act or the MOI. The right to appoint any person as a proxy is contained in the act (and the MOI contains provisions with regard to the appointment of proxies)" (para 13.3).

Having already ruled that the particular rule is in contravention with section 58 of the Act, this remark of the court can be argued to be *obiter*. Be that as it may, section 15(3) does not prohibit rules in respect of matters that already are addressed in the memorandum of incorporation or the Act, it merely provides that the rules must be necessary or incidental to governance and, in effect, must not be in respect of governance, if such is addressed in the memorandum of incorporation or the Act. If the rules are purported to be in respect of governance, and such is addressed in the memorandum of incorporation or Act, the rules will be void due to the provisions of section 15(4). Therefore, the rules may regulate the *manner* in which the proxies must be submitted, but not the *right* to appoint a proxy. The rules must also be necessary or incidental to the governance of the company, However, if the rules comply with the requirements as to "governance" as set out above, it is submitted that nothing turns on the distinction between necessary and incidental. A rule that is not necessary will be incidental and *vice versa* (see *Henochsberg* 76).

The concept of rules of and in a company and the regulation thereof in the Act, are also used in certain jurisdictions in Canada and are known as by-laws (see Welling *et al Canadian corporate law cases notes & materials* (2010) 120). Section 103(1) of the Canada Business Corporations Act RSC 1985 c C-44 ("CBCA") provides: "Unless the articles, by-laws or a unanimous shareholder agreement otherwise provide, the directors may, by resolution, make, amend or repeal any by-laws that regulate the business or affairs of the corporation." "Affairs" is defined in section 2(1) of the CBCA as "the relationships among a corporation, its affiliates and the shareholders, directors and officers of such bodies corporate, but does not include the business carried on by such bodies corporate". The principle, therefore, is that internal matters are regulated by the by-laws and that outside relationships, such as a contract with third parties, will not fall within either the power to "regulate" as in section 103(1) or the definition of "affairs" in section 2(1) of the CBCA. The practice was to incorporate as much of the provisions of the articles of association in the by-laws, as they are easier to amend (merely a board resolution) if compared to the majority required for the amendment of the articles of association (Ewasiuk "The Business Corporations Act – The distinction between bylaws and articles of association" 1983 *Alberta LR* 381–385). However, certain matters cannot, by definition, be regulated in the by-laws, one of which is a pre-emption right or a right of first refusal as it "would be an absurd situation if the directors of a corporation were allowed to fundamentally affect the ability of the shareholders, even temporarily, to deal with their shares" (*idem* 384). The Delaware General Corporation Law (8 Del C 1953) ("DGCL") provides in section 109(b) that the by-laws may contain any provision not inconsistent with the law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees. In *CA Inc v AFSCME Employees Pension Plan* 953 A2d 227 (2008) 235 the Supreme Court of Delaware said that: "It is well-established Delaware law that a proper function of bylaws is not to mandate how the board should decide specific substantive business decisions, but rather to define the process and procedures by which those decisions are made" (see also *Gow v Consol Coppermines Corp* 165 A 136 (Del Ch 1933) 140 and *Hollinger International Inc v Black* 844 A2d 1022 (Del Ch 2004) 1078–1079). Therefore, at least for purposes of this discussion, the Canadian and Delaware examples would support the principle regarding the restriction of the ambit of rules as discussed above.

2 2 Legal basis of rules

The basis of South African company law has always been accepted to be the partnership and as such the contractual nature or roots of company law has always been accepted and applied (see Delport in Visser and Pretorius (eds) *Essays in honour of Frans Malan* (2014) 81–92). In partnership law, every partner has the right to conclude contracts for and on behalf of the partnership, for purposes of the partnership business. However, this power was, at least impliedly, delegated to the board of directors in terms of the law as it stood before the 2008 Companies Act. Although this contractual division of powers was abolished by the 2008 Companies Act (see also §2 3 below), the elements of the contractual relationship remained, at least apparently. The 1973 Companies Act, which was repealed as far as it is relevant here, by the 2008 Act, provided expressly in section 65(2) that the memorandum of association and the articles of association bound each member as if signed by that member. This has been said

to illustrate the contractual nature of the memorandum and articles (Cilliers *et al* 79) but it was also recognised by the (then) appellate division in *Gohlke and Schneider v Westies Minerale (Edms) Bpk* 1970 2 SA 685 (A), albeit in respect of section 16 of Act 46 of 1926, but the wording of that section is essentially the same as section 65(2) of the 1973 Companies Act.

The 2008 Companies Act provides in section 15(6) that the company's memorandum of incorporation is binding between the company and each shareholder, between or among the shareholders of the company and between the company and each director or prescribed officer of the company, or any other person serving the company as a member of a committee of the board, but only in respect of the exercise of their respective functions within the company. Section 15(6) does not provide the basis of these relationships, but it is accepted that it is contractual in nature in the capacity of shareholder/member. The nature of the relationship, and whether it is indeed a contractual relationship, is important not only in how it is enforced but also as to the capacity in which those indicated are bound (see Cassim *Contemporary company law* 142; *Henochsberg* 28(3)). However, these aspects are not at issue in this discussion. What is important is that section 15(6) provides that the rules of a company, as in terms of section 15, fall within the same category as the memorandum of incorporation. It can therefore be accepted that the rules are also contractually binding between the parties as indicated, namely, between the company and each shareholder/member, between or among the shareholders/members of the company and between the company and each director or prescribed officer in the capacity as indicated.

2 3 Limitations of power to make rules

As stated above, the rules must be within the parameters set in section 15(3) and (4). However, the power to make rules is given to the board. In terms of section 66(1), the business and affairs of the company are managed by or under the direction of the board, except to the extent that the Act or the memorandum of incorporation provides otherwise (see *Navigator Property Investments (Pty) Ltd v Silver Lakes Crossing Shopping Centre (Pty) Ltd* [2014] JOL 32101 (WCC); *Kaimowitz v Delahunt* 2017 3 SA 201 (WCC) and *Henochsberg* 250(3)). The fact that the rules fall within the powers of the board likewise is a confirmation of the principle that the board is the highest authority in the company. The shareholders/member can ratify the rules (or not), but cannot make or amend the rules (see also discussion *infra*). The power to make rules is therefore subject to the fiduciary and other duties of the board (of directors). The fiduciary duties are as in terms of the common law, but also as prescribed in the 2008 Companies Act. It is not intended to give a definitive exposition of the fiduciary and other duties of the board (see Cassim *Contemporary company law* 524; *Henochsberg* 290(5)), and in respect of this discussion the focus is on some of the duties as in section 76, although other duties may, and will, be applicable. Section 76(3) provides, *inter alia*, that:

> "(3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director –
> (a) in good faith and for a proper purpose;
> (b) in the best interests of the company."

The board must therefore, at least, act *bona fide*, for a proper purpose and in the best interests of the company when they make, amend or repeal a rule. In respect of *bona fides* it was said in *In re Smith & Fawcett Ltd* [1942] Ch 304 (CA) 306,

[1942] 1 All ER 542 543 that the duty requires the honest exercise by the directors of their judgment as to what is in the company's interests. In *Re Halt Garage (1964) Ltd* [1982] 3 All ER 1016 (Ch) 1034 Oliver J stated that " the test of *bona fides* and benefit to the company seems to me to be appropriate, and really only appropriate, to the question of the propriety of an exercise of a power rather than the capacity to exercise it". It has been said that *bona fides* do not exist independently, and in deciding whether the duty has been observed the test will be whether in the circumstances a reasonable person could have believed that the particular act was in the interests of the company (*Charterbridge Corporation Ltd v Lloyds Bank Ltd* [1970] Ch 62, [1969] 2 All ER 1185 1194; *Howard Smith v Ampol Petroleum Ltd* [1974] 1 All ER 1126 (PC) 1133; *Visser Sitrus (Pty) Ltd v Goede Hoop Sitrus (Pty) Ltd* 2014 5 SA 179 (WCC) para 74. This creates the impression, and it was stated as such in *Visser Sitrus*, that it is one test, with a subjective (*bona fide*) and an objective (interests of the company) element. For purposes of this discussion it is accepted that this is correct, as the focus here is on the objective elements of these fiduciary duties, namely, that it must be for a proper purpose and in the best interests of the company. If the board makes, amends or repeals a rule, it therefore must be for a proper purpose and in the best interests of the company. In *Visser Sitrus* para 75 the court said that section 76 requires "the *bona fide* assessment of the directors to have a rational underpinning" and refers, *inter alia*, to the *Charterbridge Corporation Ltd* case above where the court said (1194) that:

> "The proper test, I think, in the absence of actual separate consideration, must be whether an intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transaction was for the benefit of the company."

This *dictum* was preceded by the statement that in *ultra vires* actions the state of mind of the bank's directors is irrelevant and is therefore clearly *obiter*. The court in *Visser Sitrus* then proceeded to apply the pure "rationality" principle (not with the subjective elements as in the test for best interests of the company) as in administrative law in respect of the proper purposes test. The court referred to the *dictum* in *Pharmaceutical Manufacturers Association of SA: In re Ex parte President of the Republic of South Africa* 2000 2 SA 674 (CC) para 90 in this context and said (para 78), without any reference to company law judgments, that these principles relating to rationality can be applied, with modifications, to the rationality requirement in respect of the proper exercise of their powers (see Stevens and De Beer "The duty of care and skill, and reckless trading: Remedies in flux?" 2016 *SA Merc LJ* 250–284 for the effect of this interpretation on the "business judgment" rule in section 76(4)(a)). The conclusion (para 80) was that the proper purpose test in section 76(3)(a) is purely objective and that the overarching purpose for which the directors must exercise their powers is the purpose of promoting the best interests of the company. It is not intended to discuss this reasoning of the court, but two remarks may be necessary. In the first instance the statement that one of the reasons for joining the subjective duty to act *bona fide* (honestly) with the (objective) requirement that the act must be in the interests of the company, is the application of one of the elements of the "business judgment" rule in section 76(4)(a)(iii), that the director had a rational basis for believing, and did believe, that the decision is in the best interests of the company (*Visser Sitrus* paras 73 74). However, this requirement only serves to "prove" that the director acted in accordance with section 76(3)(b) (best interests of the company) and section 76(3)(c) (care, skill and diligence), and does not

speak to *bona fides* as contained in section 76(3)(a). In the second instance it should be noted that in *Eclairs Group Limited v JKX Oil & Gas plc* [2015] UKSC 71 the Supreme Court of the United Kingdom said that the "proper purpose" test is not objective but subjective, as the motive in the exercise of the powers must be determined (para 15 and see Langford and Ramsay "The proper purpose rule as a constraint on directors' autonomy – *Eclairs Group Limited v JKX Oil & Gas plc*" 2017 *MLR* 110–132).

The (substantive) content of the rules, especially before ratification, may also be subject to other requirements, apart from the "fiduciary duty test". The reason for this is that the nature of the rules is contractual (see §2 3 above) and the unilateral creation of those rules by the board, up to at least ratification, may be subject to contract law principles, as influenced by constitutional imperatives. Although the rules might irk one's "individual sense of propriety and fairness" because of their restrictive and regimented nature, they cannot be said to be contrary to public policy and, because the framework for the rules is a (private) contractual relationship, the Promotion of Administrative Justice Act 3 of 2000 does not apply (*Singh v Mount Edgecombe Country Club Estate Management Association* (*RF*) *NPC* 2016 5 SA 134 (KZD) paras 81 82). In *Barkhuizen v Napier* 2007 5 SA 323 (CC) para 36 the Constitutional Court accepted that the approach is to determine whether a particular clause in a contract (and therefore a rule as well) is inimical to the "values that underlie our constitutional democracy . . . and thus contrary to public policy".

The power to make rules lies exclusively with the board, and the shareholders/members cannot be given that power (s 66(1) of the Act provides for delegation of powers by the board, but the responsibility and obligations remain with the board. See *Henochsberg* 250(6) and authorities cited. The Model Business Corporation Act of the American Bar Association ("MBCA") provides in section 10.20b that the board and the shareholders have the power to make and amend rules. Delaware, on the other hand, which was apparently the model for the provisions in the 2008 Companies Act, provides in section 109(a) of the DGCL that any corporation may, in its certificate of incorporation, confer the power to adopt, amend or repeal bylaws (rules) upon the directors. See also *American Int'l Rent a Car Inc v Cross* 1984 WL 8204 (Del Ch 1984); *General DataComm Industries Inc v State of Wisconsin Investment Board* 731 A2d 818, 821 n1 (Del Ch 1999) and *Centaur Partners IV v National Intergroup Inc* 582 A2d 923 929 (Del 1990)).

In terms of section 15(4)(b) of the Act, a rule takes effect on a date that is the later of 10 business days after the rule is filed in terms of section 15(3)(b), or the date, if any, specified in the rule. Section 15(4)(c) provides that the rule is binding on an interim basis from the time it takes effect until it is put to a vote at the next general shareholders meeting of the company and then on a permanent basis only if it has been ratified. If the board makes or amends a rule and does not comply with its duties to act *bona fide*, in the best interests of the company and for a proper purpose, the remedies are for breach of fiduciary duties towards the company, amongst others in terms of section 77 and also the statutory derivative action in terms of section 165 of the Act. A shareholder or shareholders not acting as the company, cannot hold the board liable as the fiduciary duties are owed to the company (*Foss v Harbottle* (1843) 2 Hare 461, 67 ER 189; and see in particular the analysis of this principle, and the relevant cases, in *Letseng Diamonds Ltd v JCI Ltd; Trinity Management* (*Pty*) *Ltd v Investec Bank Ltd* 2007 5 SA 564 (W) 573–574), unaffected in this regard by the reversal of this judgment on appeal

in *Letseng Diamonds Ltd v JCI Ltd* 2009 4 SA 58 (SCA); *Trinity Asset Management (Pty) Ltd v Investec Bank Ltd* 2009 (4) SA 89 (SCA); *Mbethe v United Manganese of Kalahari (Pty) Ltd* 2016 5 SA 414 (GJ); *Lewis Group Ltd v Woollam (1)* [2017] 1 All SA 192 (WCC)). On the rights of a shareholder, see also *Communicare v Khan* 2013 4 SA 482 (SCA); *Itzikowitz v ABSA Bank Ltd* 2016 4 SA 432 (SCA) para 16; *Johnson v Gore Wood & Co* [2001] 1 All ER 481 and *Henochsberg* 78(7) on the question whether a shareholder can act on the basis of contract law). If the rules are ratified by the majority, it will not exclude or ratify, even if so contemplated, the possible breach of fiduciary duties of the board towards the company (see s 78 of the Act and *Henochsberg* 308). Shareholders, acting as a body, do not have a fiduciary duty to the company, but ratification by the majority decision in a general meeting can be actionable in terms of the common law if it is fraud on the minority and also under the circumstances as in section 163 of the Act (see *Henochsberg* 587 and 573 respectively).

The rules of a (NPC homeowners' association) company were the subject of litigation in, amongst others, *Abraham v Mount Edgecombe Country Club Estate Management Association Two (RF) (NPC)* (7124/12) [2014] ZAKZDHC 36 (17 September 2014) and *Singh v Mount Edgecombe Country Club Estate Management Association* (*RF*) *NPC* 2016 5 SA 134 (KZD) (both companies were, for some reason, RF companies, but this is not significant in this context). In *Abraham* the rules provided that dogs that did not comply with certain restrictions as to size and weight may not be brought onto the estate. The court found (para 46) that the directors did not have a discretion in terms of the rules to allow dogs that do not comply with the restrictions and the exclusion of a dog that did not comply with the restrictions as in the rule was valid. If the board has a discretion, in the true sense of the word, then that discretion must be exercised according to its fiduciary and other duties (see *South African Fabrics Ltd v Millman* 1972 4 SA 592 (A) 596; *Visser Sitrus*; *Dawood, Shalabi and Thomas v Minister of Home Affairs* 2000 3 SA 936 (CC) para 53 and *Henochsberg* 75). In *Singh* the rules contained certain restrictions, such as a speed limit within the estate and restriction as to movement of employees in the estate and provisions in respect of the enforcement actions by the homeowners' association when the rules were not complied with. In both *Abraham* and *Singh* the particular court found that the rules were based on a contractual relationship (*Abraham* para 23 and *Singh* para 10). The court in *Singh* said that the only question was whether these restrictive rules in the contractual relationship were "unlawful and ought therefore to be regarded as *pro non scripto*" (para 12). With reference to, *inter alia*, *Sasfin (Pty) Ltd v Beukes* 1989 1 SA 1 (A) 9 and the principles laid down in *Botha (now Griessel) v Finanscredit (Pty) Ltd* 1989 3 SA 773 (A) 783 and *Juglal v Shoprite Checkers (Pty) Ltd t/a OK Franchise Division* 2004 5 SA 248 (SCA) para 12, the court found that the rules were not unlawful (*Singh* para 82), but that the "contractual right" of enforcement actions by the homeowners' association in the transgression of the rules was not provided for in the rules (para 85). *Abraham* and *Singh* referred to various judgments in respect of rules in terms of a sectional title scheme (see *Abraham* para 43). The principles in respect of these rules and the basis of these rules do not apply in respect of the Companies Act and are not authority (see § 1 above). In both judgments, the courts referred to the contractual nature of the rules due to the fact that in buying property the member agreed in the purchase contract to be subject to the rules. This is questionable, because although the rules are contractual in nature, this is because of the application of section 15, and not due to incorporation by reference in the contract for the

purchase of property. Section 15 of the Companies Act cannot be excluded by contract, and there is no indication in any of the cases that the power to make rules has been excluded, actually the contrary is clear. No reference is made in any of the cases to section 15 of the Companies Act and the requirements in respect of the power to make the rules and the requirements for the validity of the rules and there is no indication why the courts were of the opinion that these were not relevant. Inclusion of the rules as a contractual term in the purchase contract can maybe add to or confirm the contractual nature of the rules, but section 15 will still apply (see §1 above).

3 Conclusion

Under the 1973 Companies Act, company rules were used in companies in terms of the common law. The 2008 Companies Act now provides that the board may make rules, unless that power is excluded in the memorandum of incorporation. Company rules in terms of the 2008 Companies Act are subject to various restrictions and requirements as provided for in section 15 of the 2008 Companies Act, and these restrictions or requirements cannot be amended by the memorandum of incorporation, much less by separate contract. The power to make, amend or repeal rules, in addition, is similarly subject to the fiduciary duties of directors, such as in section 76(3), to act *bona fide*, in the interests of the company and to act for a proper purpose, and due to the contractual nature of the rules, also to the common law principles of the law of contract. Ratification of the rules by the general meeting of the company as required by section 15(5) will not rectify breaches of fiduciary duties of directors in making or amending a rule, and such ratification must also comply with the general requirements in the common law and the Companies Act in respect of the (proper) exercise of the power of the majority. Although rules were/are popular due to the fact that making and amending of the rules were usually perceived to be easier and quicker than amendments to a shareholders' agreement or the memorandum of association, there are onerous requirements on different levels of the company that must be complied with. Failure to comply with these requirements will have the effect that the rule is void.

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