Corporate Governance Series
The Companies Act, 2008

May 2009

Steering point

The Companies Act, 2008 [No 71 of 2008] ("the Act") was signed into law on 8 April 2009. The Act constitutes the rewrite of the Companies Act, 1973[1]. The effective date of the Act is yet to be determined by the President by proclamation in the Gazette. This date may not be earlier than one year following the date on which the President assented to the Act, and is anticipated to be 1 July 2010.

In this Steering Point we discuss the provisions of the Act affected by financial reporting as they apply to:

[1] References to the Companies Act, 1973 include amendments by the Corporate Laws Amendment Act, 2006

PricewaterhouseCoopers

Categorisation of companies

The Act provides for the determination of the following categories of companies:

- "non-profit" companies identified as "NPC" (previously 'Section 21'), and
- "profit" companies that can be either:
  - "public companies" identified as "Limited" or "Ltd";
  - "state-owned companies" identified as "SOC Ltd";
  - "private companies" identified as "Proprietary Limited" or "(Pty) Ltd"; or
  - "personal liability companies" identified as "Incorporated" or "Inc"

The "widely held" and "limited interest" definitions imposed by the Corporate Laws Amendment Act, 2006 (the "CLAA") will no longer apply.

The following is a schematic presentation of the categories of companies in terms of the Act:

Categories of companies

Profit company

A company incorporated for the purpose of financial gain for its shareholders.

Non-profit company

a. A company incorporated for a public benefit or other object as required by item 1(1) of Schedule 1; and

b. the income and property of which are not distributable to its incorporators, members, directors, officers or persons related to any of them except to the extent permitted by item 1(3) of Schedule 1.

State-owned company

An enterprise registered in terms of this Act as a company and either

(a) falls within the meaning of "state-owned enterprise" in terms of the Public Finance Management Act, 1999; or

(b) is owned by a municipality, as contemplated in the Local Government Municipal Systems Act, 2000 and is otherwise similar to an enterprise referred to in paragraph (a).

Private company

A profit company that

(a) is not a state-owned company or a personal liability company; and

(b) its Memorandum of Incorporation

(i) prohibits it from offering any of its securities to the public and

(ii) restricts the transferability of shares.

Personal liability company

A company that meets the criteria for a private company, whose Memorandum of Incorporation states that the company is a personal liability company.

Public company

A profit company that is not a state-owned company, a private company or a personal liability company.

Subsidiaries of public companies are classified in accordance with the definitions of the various categories. Subsidiaries of public companies will therefore not neccessarily also be classified as public companies.

Audit committees: Appointment, membership and qualifications – comparison with the Companies Act, 1973

	Companies Act, 2008	Companies Act, 1973
Appointment of audit committee	An audit committee must be elected at each annual general meeting.	In every financial year in which a company is a widely held company, its board of directors must appoint an audit committee for the following financial year.
Category(ies) of companies that are required to have an audit committee	Public companies, state-owned companies or other companies that have voluntarily elected to have an audit committee.	Widely held companies.
Exemption from appointing an audit committee	Similar to the Companies Act, 1973.	Widely held companies are exempted from appointing an audit committee if the audit committee of a holding company will perform the functions on behalf of that company. The Minister may by publication in the Gazette specify certain categories of companies that are not required to appoint an audit committee.
Number of members	At least three members are required.	At least two members are required.
Membership	Each member of the audit committee must be a director of the company.	The audit committee must consist only of non-executive directors of the company who must act independently.
Qualification of members	Each member must not be - (i) involved in the day to day management of the company's business or have been so involved at any time during the previous financial year; (ii) a prescribed officer or full-time employee of the company or another related or inter-related company, or have been such an officer or employee at any time during the previous three financial years; (iii) a material supplier or customer of the company, such that a reasonable and informed third party would conclude in the circumstances that the integrity, impartiality or objectivity of that director is compromised by that relationship; or related to an individual in (i) to (iii).	A director is a non-executive director of a company if the director— (i) is not involved in the day to day management of the business and has not in the past three financial years been a full-time salaried employee of the company or its group; (ii) is not a member of the immediate family of an individual mentioned in (i). A director acts independently if that director— (i) expresses opinions, exercises judgment and makes decisions impartially; (ii) is not related to the company or to any shareholder, supplier, customer or other director of the company in a way that would lead a reasonable and informed third party to conclude that the integrity, impartiality or objectivity of that director is compromised by that relationship.
Qualifications for audit committee members prescribed by the Minister	The Minister may prescribe minimum qualification requirements for members of an audit committee as necessary to ensure that any such committee, taken as a whole, comprises persons with adequate relevant knowledge and experience to equip the committee to perform its functions.	No provision for the prescription of qualifications by the Minister.

Functions of the audit committee in terms of the Companies Act, 2008

Neither the appointment nor the duties of an audit committee reduce the functions and duties of the board or the directors of the company except with respect to the appointment, fees and terms of engagement of the auditor. The audit committee is appointed by the shareholders at the annual general meeting.

<table>
<tr>
<th>Functions relating to the terms of engagement of the auditor</th>
<th>Functions relating to non-audit services performed by the auditor</th>
<th>General functions</th>
</tr>
<tr>
<td>The audit committee is required to –

• nominate for appointment as auditor of the company a registered auditor who, in the opinion of the audit committee, is independent of the company;

• determine the fees to be paid to the auditor and the auditor’s terms of engagement; and

• ensure that the appointment of the auditor complies with the Act and any other legislation relating to the appointment of auditors.</td>
<td>The audit committee is required to –

• determine the nature and extent of any non-audit services that the auditor may provide to the company, or that the auditor must not provide to the company, or a related company; and

• pre-approve any proposed agreement with the auditor for the provision of non-audit services to the company.</td>
<td>The audit committee is required to –

• receive and deal appropriately with any concerns or complaints, whether from within or outside the company, or on its own initiative relating to:
– the accounting practices and internal audit of the company;
– the content or auditing of the company’s financial statements;
– the internal financial controls of the company; or
– any related matter;
• to make submissions to the board on any matter concerning the company’s accounting policies, financial control, records and reporting; and

• to perform other functions determined by the board, including the development and implementation of a policy and plan for a systematic, disciplined approach to evaluate and improve the effectiveness of
– risk management;
– control; and
– governance processes within the company.</td>
</tr>
<tr>
<td colspan="3">The audit committee is required to prepare a report to be included in the annual financial statements -

• describing how the audit committee carried out its functions;

• stating whether or not the audit committee is satisfied that the auditor was independent of the company; and

• commenting in any way the committee considers appropriate on the financial statements, the accounting practices and the internal financial control of the company.</td>
</tr>
</table>

A company must pay all expenses reasonably incurred by its audit committee including, if the audit committee considers it appropriate, the fees of any consultant or specialist engaged by the audit committee to assist it in the performance of its functions.

The requirement for audit or review of different categories of companies

Categories of companies

Profit company

Non-profit company

Must prepare annual financial statements

Audited voluntarily at the option of the company; or

Independently reviewed in a manner that satisfies the regulations made in terms of S 30(7)

State-owned company

Must prepare annual financial statements.

Must appoint an auditor (S 90).

Requirements of the Public Audit Act, 2004 will prevail if in conflict with Chapter 3 of the Act.

Private company

Must prepare annual financial statements.

Audit required only if prescribed by regulation made in terms of S30(7); or

Voluntarily audited at the option of the company; or

Independently reviewed in a manner that satisfies the regulations made in terms of S30(7) unless exempted.

Exempt from being independently reviewed if

(a) one person holds, or has all of the beneficial interest in, all of the securities issued by the company; or

(b) every person who is a holder of, or has a beneficial interest in, any securities issued by the company is also a director of the company unless the company has only one director and that director is a person disqualified to act as a director.

Personal liability company

Must prepare annual financial statements.

Audited voluntarily at the option of the company; or

Independently reviewed in a manner that satisfies the regulations made in terms of S 30(7).

Public company

Must prepare annual financial statements.

Must be audited.

S 30(7): The Minister may make regulations, including different requirements for different categories of companies, prescribing:

(a) the categories of any private companies that are required to have their respective annual financial statements audited taking into account whether it is desirable in the public interest, having regard to the economic or social significance of the company as indicated by

(i) its annual turnover;

(ii) the size of its workforce; or

(iii) the nature and extent of its activities

and

(b) the manner, form and procedures for the conduct of an independent review other than an audit, as well as the professional qualifications, if any, of a person who may conduct such reviews.

Such regulations must still be issued.

Auditor rotation – comparison with the Companies Act, 1973

	Companies Act, 2008	Companies Act, 1973
Applicable categories of companies	Auditor rotation applies to public companies and state-owned companies except to the extent that the company has been granted an exemption by the Minister.	Audit rotation applies to widely held companies.
Rotation period	Similar to the Companies Act, 1973.	The same individual may not serve as the auditor or designated auditor for more than five consecutive financial years.
"Cooling-off" period	Similar to the Companies Act, 1973.	Where an individual has served as the auditor or designated auditor for two or more consecutive financial years and then ceases to be the auditor or designated auditor, the individual may not be appointed again as the auditor or designated auditor of that company until after the expiry of at least two further financial years.
Joint audits	If a company has appointed two or more persons as joint auditors, the company must manage the rotation required by this section in such a manner that all of the joint auditors do not relinquish office in the same year.	No provisions exist regarding rotation of auditors where auditors are jointly appointed.

Accounting records

A company must keep accurate and complete accounting records in one of the official languages of the Republic. Accounting records must be kept in the prescribed manner and form.

It is an offence for a company

- with an intention to deceive or mislead any person, to fail to keep accurate or complete accounting records or to keep records other than in the prescribed manner and form; or
- to falsify any of its accounting records, or permit any person to do so.

It is an offence for any person to falsify a company's accounting records.

Financial reporting standards

The Act requires that any financial statements prepared by a company must satisfy financial reporting standards.

The Minister may prescribe financial reporting standards after consulting with the Financial Reporting Standards Council. This provision contrasts with the current provisions in the Companies Act, 1973 in terms of which the Financial Reporting Standards Council is empowered to set accounting standards in South Africa. We regard the standard-setting model under the CLAA as preferable as a standard-setting body should be able to react quickly to the voluminous changes to International Financial Reporting Standards (IFRS) to ensure that financial reporting standards in South Africa are continually aligned with international standards.

Financial reporting standards must be consistent with IFRS of the International Accounting Standards Board.

The Minister may establish different standards applicable to profit and non-profit companies and different categories of profit companies.

Close Corporations

The Act provides for the indefinite continued existence of the Close Corporations Act, 1984, but provides for the closing of that Act as an avenue for incorporation of new entities, or for the conversion of companies into close corporations, as of the effective date of the Act.

Annexure A

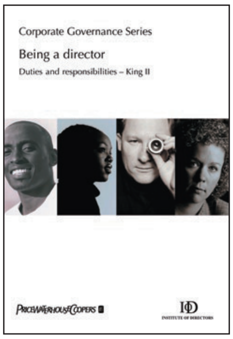
Comparison of other key administrative and financial reporting areas with the Companies Act, 1973

The following table represents a high level comparison of key administrative and financial reporting areas between the Companies Act, 2008 [No. 71 of 2008] and the Companies Act, 1973 [No. 61 of 1973].

The Companies Act, 2008	The Companies Act, 1973
Administration and enforcement	
• Companies and Intellectual Property Commission (CIPC)	• Companies Registration Office (in practice CIPRO) • Financial Reporting Investigations Panel (FRIP)
• Commissioner of the Commission	• Registrar of Companies
• Companies Tribunal	
• Takeover Regulation Panel (TRP)	• Securities Regulation Panel
• Takeover Special Committee	
• Financial Reporting Standards Council (FRSC)	• Financial Reporting Standards Council (FRSC)
Formation of a company	
• Memorandum of incorporation (MOI)	• Memorandum of association
• Rules of a company	• Articles of association
Unregistered associations and partnerships	
• No limitation on number of partners or persons	• **S 30** Maximum of 20 persons for any unregistered business/ association/ partnership, carrying on business for gain, except for designated organised professions.
• **S 8(3)** Unregistered associations of persons, carrying on business for gain, are not corporate bodies.	• **S 31** Unregistered associations, carrying on business for gain, are not corporate bodies.
Types of companies	
• Types of companies – Profit company (minimum 1 founding person) – Non-profit company (minimum 3 founding persons)	• Types of companies – Company with share capital (minimum 7 founding persons for public company/ 1 for private company) – Company limited by guarantee (minimum 7 founding persons)
Categories of companies	
• Profit companies	
– Public (minimum 1 member)	• Public (minimum 7 members)
– Private (minimum 1 member)	• Private (maximum 50 members)
– Personal Liability (minimum 1 member)	• Section 53(b) private company (memorandum states that directors & past directors are jointly & severally liable with company for debts & liabilities)
– State-owned company	
• Non-profit companies (not required to have members unless provided for by its Memorandum of incorporation).	• Section 21 (associations not for gain)
	• Widely held (public and specifically scoped in companies) • Limited interest (companies other than widely held)
Names	
• **S 11**	• **S 49**
• {Profit company – Public} – “Ltd”	• {Public company} – “Ltd” • {Company limited by guarantee} – “(Limited by Guarantee)”
• {Profit company – Private} – “(Pty) Ltd”	• {Private company} – “(Pty) Ltd”
• {Personal liability company} – “Inc.”	• {Organised profession} – “Inc.”
• {Non-profit company} – “NPC”	• {Section 21 company} – “Association incorporated under section 21”
• {State-owned company} – “SOC Ltd” and, where applicable: • {Profit company name is the registration number only} – “(South Africa)” • {Company with MOI containing special conditions} – “(RF)”	
Directors	
• Public (minimum 3)	• Public (minimum 2)
• Private (minimum 1)	• Private (minimum 1)
• Personal Liability (minimum 1)	
• Non-profit (minimum 3)	

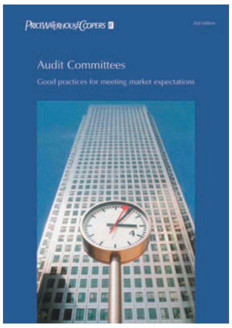
The Companies Act, 2008	The Companies Act, 1973
Shares • Par value shares only allowed for existing companies until the Minister, by regulation, provides for conversion to no par value shares. • No par value shares	• Par value (with share premium where applicable) • No par value (stated capital) • No shares issued (limited by guarantee)
External companies • **S 23** External company must register.	• **S 322** External company must register.
Distributions to shareholders • **S 46** Resolution by directors, specifically acknowledging application and compliance with the solvency and liquidity test.	• **S 90** Authorisation by articles and complying with solvency and liquidity requirements.
Share buybacks • **S 48** Resolution by directors, specifically acknowledging application and compliance with the solvency and liquidity test.	• **S 85** Authorisation by articles and special resolution. Compliance with solvency and liquidity requirements.
Financial statements • **S 29(1)** Compliance with financial reporting standards. • **S 30** All companies must prepare annual financial statements within six moths of its financial year end, which must be approved by the board and presented to the first shareholders meeting after such approval. • **S 29(3)** Summary financial statements may be issued.	• **S 285A(1)** Widely held companies must comply with financial reporting standards. • **S 285A(2)** Limited interest companies must comply with specifically developed standards. • **S 286** Directors to cause annual financial statements to be prepared, in respect of all companies, and presented to the annual general meeting (AGM).
Audit of financial statements • **S 90** Public and State-owned companies to appoint an auditor • **S 30** Other companies to be either audited or independently reviewed dependent on certain measures. • **S 30** Sole shareholder/director private companies exempted from review.	• **S 300** All companies to be audited.
Attendance of auditors • No requirement for the auditor to meet with the audit committee, prior to the board meeting, to approve the financial statements • No requirement for the auditor to attend the AGM	• **S 300A(1)** Auditor must meet with the audit committee of a widely held company not more than one month before the board meets to approve the financial statements • **S 300A(2)** Auditor must attend every AGM of a widely held company where the financial statements are to be considered
Disposal of assets • **S 115** Special resolution to dispose of > 50% of assets or business, merge or implement a scheme of arrangement, subject to minimum requirements (subsidiary's disposal scoped in).	• **S 228** Special resolution to dispose of > 50% of assets or business (subsidiary's disposal scoped in). • **S 311** Compromise and arrangement requires majority of 75% in value of creditors/members.
Financial assistance to purchase shares • **S 44(3)(a)(ii)** Special resolution and complying with solvency and liquidity requirements.	• **S 38(2A)** Special resolution and complying with solvency and liquidity requirements
Loans to directors • **S 45(3)(a)(ii)** Special resolution for a specific director or generally for a potential director and complying with solvency and liquidity requirements.	• **S 226(2)(a)** Special resolution or prior consent of all members.
Business rescue and compromise with creditors • **Chapter 6**	**Judicial management** • **Chapter XV**

Publications available from the PricewaterhouseCoopers Library and Information Centre on corporate governance:



Being a director, Duties and Responsibilities – King II

The publication covers the duties and responsibilities of directors for the effective governance of their companies.

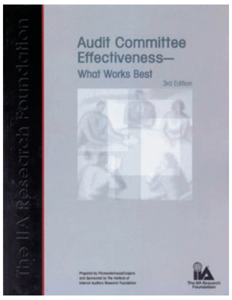


2003 – Audit Committees - Good practices for meeting market expectations (2nd edition)

The 2nd edition of our global guide on Audit Committees summarises best practices and requirements in over 40 countries. It covers all aspects of an audit committee's work, including: organisation (terms of reference, membership, meetings): key responsibilities; communicating and reporting by the committee; and evaluating audit committee effectiveness.

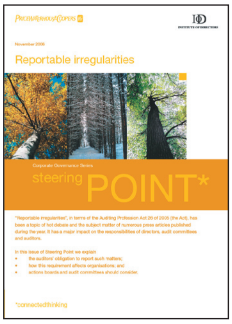
2006 - Current developments for audit committees

In addition to supporting the role of audit committee oversight of Section 404 of the US Sarbanes-Oxley Act, this publication highlights some of the other significant governance developments and their implications to help audit committees cope with ongoing regulatory, legislative and other changes in the business environment.



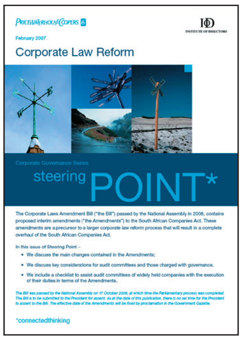
2005 – Audit committee effectiveness - What works best (3rd edition)

The report captures how leading audit committees are effectively and thoughtfully discharging their expanded duties. It also provides numerous examples of how leading audit committees are not just complying with, but surpassing, requirements.



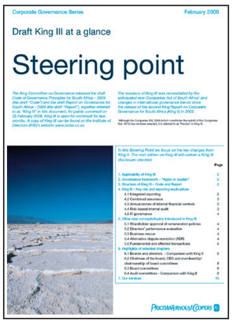
Steering Point - November 2006

This edition explains the auditor's obligations to report "reportable irregularities" and examines how the requirement to report affects organisations and more specifically boards and audit committees.



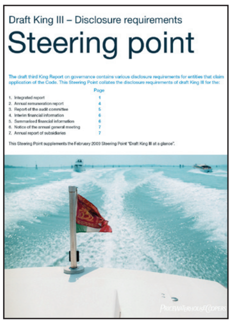
Steering Point - February 2007

This edition summarises the main changes contained in the Corporate Laws Amendment Bill, 2006. It discusses the key considerations for audit committees and those charged with governance.



Steering Point – February 2009

This edition covers the key risk and reporting implications of draft King III for companies, boards and audit committees. It contains highlights from the "Boards and Directors" and "Audit Committees" chapters.



Steering Point – March 2009

This edition supplements the February 2009 Steering Point "Draft King III at a glance". It collates the disclosure requirements of Draft King III for the integrated report, annual remuneration report, report of the audit committee, interim financial information, notice of the AGM and annual report of subsidiaries.

For further information on these and other publications, please contact your engagement partner or the PricewaterhouseCoopers Library and Information Centre at +27 (11) 797 5062.

www.pwc.com