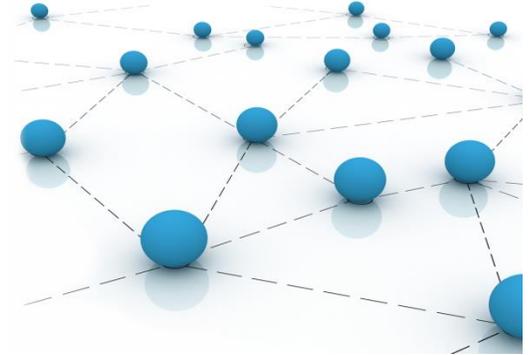


## The Companies Act Private companies need to verify their classification



### Some private companies are in fact public companies

In order for companies to ensure compliance with all relevant provisions of the Companies Act (the Act), it is important that the company be classified correctly. The classification may affect provisions related to, among others, governance, the audit requirement, independent review, the audit committee, financial reporting standards and fundamental transactions.

During the transitional period (1 May 2011 to 30 April 2013) the Act provided that in the event of a conflict between a company's Memorandum of Incorporation (MOI) (previously the Memorandum and Articles of Association) and the Act, the provisions of the MOI prevailed. This also applied to a conflict pertaining to the company's classification. As a result, it often happened that a company may be identified as a private company by its MOI, but was classified as a public company in terms of the Act. During the transition period such companies were able to rely on the classification as per the MOI, and continued to operate as private companies. However, since the end of the transition period (namely 1 May 2013), the provisions of the Act override those of the MOI. **This means that companies that regard themselves as private companies may in fact be either public companies or state owned companies.**

It is important to note that in certain instances the classification will be done by default, i.e. where a "private company" does not meet the requirements of the Act, it will automatically be classified as a public company. Similarly, the classification will be automatic where a company meets the requirements for classification as a state owned company.

### Classification of companies

#### Different forms of companies

In terms of the Act, companies are classified as either profit companies or non-profit companies. Non-

profit companies, which are the successors to the old section 21 companies, have to comply with a set of principles set out in Schedule 1 of the Act. These principles relate mainly to the purpose or objectives and policies of the company, matters related to directors and members, fundamental transactions and the winding up of non-profit companies. Also, the Act exempts non-profit companies from certain provisions of the Act.

With regard to profit companies, the Act distinguishes between four different types of companies, namely:

- **Private companies ((Pty) Ltd):** A company that is not a state owned company, and its MOI prohibits it from offering any of its securities to the public, and restricts the transferability of its securities.
- **Personal liability companies (Inc.):** A private company of which the MOI determines that the company and the directors are jointly and severally liable for any debts and liabilities of the company.
- **State owned companies (SOC Ltd.):** An enterprise, registered as a company, which is listed as a public entity in Schedule 2 or 3 of the Public Finance Management Act (the PFMA), or is owned by a municipality.
- **Public companies (Ltd.):** A company that is not a state owned company, private company or personal liability company.

### Private companies vs. public companies

In order to determine whether or not a company is classified as a private company, one has to consult its MOI. A company can ONLY be classified as a private company if its MOI contains provisions prohibiting it from offering any of its securities to the public, and restricts the transferability of its securities. Where the MOI of a private company does not contain both of these provisions it is automatically classified as a public company.

In this regard the following should be noted:

- Companies should ensure that the MOI refers to 'securities' rather than 'shares'. The requirements of the Act pertain to securities, which includes both shares and debt instruments. Thus, where the MOI prohibits the company from offering any of its 'shares' to the public, and restricts the transferability of its 'shares', it may fall foul of the requirements.
- 'Private' companies with listed debt are classified as public companies.
- The required provisions must be contained in the MOI of the company. Where such provisions are included in a shareholders agreement and not in the MOI, the company is classified as a public company.
- Where a public company wants to change its classification, an amendment of the MOI is required. The inclusion of the required provisions should be approved by a special resolution of shareholders, and the company needs to submit a form CoR 15.2 to the Companies and Intellectual Property Commission.

## Private companies vs. state owned companies

An enterprise is classified as a state owned company if it is:

- Registered as a company, and
- Is listed as a public entity in Schedule 2 or 3 of the PFMA.

Schedule 2 and Schedule 3 of the PFMA contain lists of specific types of public entities. At the end of each list is a provision stating that *all subsidiaries* of the listed entities are included in the list. This has the effect that all subsidiaries of listed entities are themselves classified as state owned companies. It is not possible for a subsidiary of a listed entity to be classified as a private company. The reason for this is that such subsidiary will meet both requirements for classification as a state owned company, i.e. it is registered as a company and it is listed in Schedule 2 or 3 of the PFMA.

However, a non-profit company cannot be a state owned company. Where a non-profit company is a subsidiary of a state owned company, such company will remain a non-profit company. This is so because only 'profit companies' are classified as private, public personal liability or state owned companies. This classification does not apply to non-profit companies.

### Conclusion

Companies need to confirm the correct classification as per the Companies Act. Some companies may have relied on the effect of the transitional provisions in order to perpetuate its classification in terms of the old Act. However, since the end of the transitional period, the provisions of the Act will supersede those of the company's MOI and as such companies may now be classified in a different category.

The incorrect classification of a company may affect the audit requirements, audit committee requirements, number of directors required, specific governance requirements, whether or not an annual general meeting is required, the required financial reporting standards, the application of the provisions pertaining to fundamental transactions and the Takeover Regulations, etc.

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Queries: Dr Johan Erasmus – [jerasmus@deloitte.co.za](mailto:jerasmus@deloitte.co.za)

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