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## Looking out for the little guy

Appraisal rights may not have been welcomed by large institutions and corporate executives, but they have an important role to play in shaping an effective and fair market.



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By [Ann Crotty](#)

When appraisal rights were first introduced into South African law in 2011, shareholder activists hailed them as a much-needed way to counter the overwhelming power of large shareholders in big deals.

Inevitably, these majority shareholders, executives and their advisers weren't thrilled by the development. And with every appraisal action that followed, they became less thrilled.

But judging from a recent article by one of the country's top corporate law experts, appraisal actions – including appraisal arbitrage – have a valuable role to play in shaping an effective and fair market.

It's easy to understand the corporate establishment's unhappiness about appraisal rights. After all, this innovation is designed to challenge the plans of boards and controlling shareholders – individuals who aren't accustomed to being challenged at all.

As Maleka Femida Cassim explains in the latest issue of the *South African Law Journal*, appraisal rights give minority shareholders the right to force a company to buy out their shares at a price reflecting their “fair value” when they dissent from transactions which have been approved by a special resolution of the shareholders.

These shareholders cannot prevent the triggering transaction, so this gives them the right “to exit from the company by withdrawing the fair value of [their] shares in cash”, writes Cassim, who is a professor in the mercantile law department at the University of South Africa.

So far, it all sounds rather academic. But the cases she refers involve one shareholder activist in particular: Albie Cilliers.

Cilliers has been the protagonist in most of the appraisal cases launched since the Companies Act, which makes this possible, came into force.

Though, as it happens, the longest outstanding case of this sort was brought by investment management firm Rozendal Partners against Capital Appreciation's share buyback in 2019. That case – delayed by an almighty legal tussle between the firms – is still in the high court awaiting a determination of the “fair price”.

The fact that there are relatively few parties prepared to launch appraisal actions is less an indication of the “fairness” of fundamental transactions in South Africa and more about how complex and risky the process is for activists. So complicated that even some of the major, well-resourced investment banks have botched the process.

It is also about how relatively small the local investment community is, and the dangers of irritating the powerful players.

‘Abusing’ appraisal rights

Cilliers knows only too well what happens when you anger the corporate establishment.

In March 2023, the extent of resentment at this innovation broke into the open when food group RCL issued an unprecedented announcement attacking Cilliers. RCL, which was smarting after a successful appraisal claim by Cilliers, slammed the activist for abusing the appraisal remedy to make profits on RCL's repurchase of its BEE shares. He had bought the shares after the repurchase details had been announced.

While RCL rightly pointed out that Cilliers' actions had not been illegal, the company argued the way he used it “could not have been the intention of the appraisal rights remedy in the act”.

RCL and other companies targeted by Cilliers' activism (African Phoenix Investments, PSG/Zeder and Arrowhead Properties) have been particularly irked by what they refer to as "appraisal arbitrage".

This is where Cilliers bought shares after the transaction has been announced, with the intention of exercising the appraisal rights as he considered the transaction price inadequate. Corporate executives and investment bank advisers call this "opportunism" and claim it's not what the act intended. They want the appraisal remedy to be restricted to pre-existing shareholders.

Cassim thinks otherwise.

"Appraisal-rights arbitrage is a potentially valuable governance tool," she writes. "A credible threat of appraisal – or the mere existence of a robust and effective appraisal remedy – serves an important governance purpose. It deters directors and controlling shareholders from succumbing to the temptation to ignore opportunistically the interests of the company's shareholders in favour of their own interests when negotiating fundamental transactions."

It also curbs bad business judgment by boards of directors.

Backing the activists

So far, judges in these cases have tended to back the activists and their use of appraisal arbitrage, calling it a social utility.

In the Arrowhead case, for instance, the judge said the appraisal right can act as "an effective back-end market check on abuses by corporate managers, controlling shareholders (and) other insiders in merger transactions".

It also acts as a check on expropriation from minority shareholders because "when a merger takes place at a fair price, appraisal arbitrage will not be attractive".

Given that the complexity of the process is likely to discourage many of the aggrieved small shareholders, Cilliers and others who do use this mechanism should be encouraged.

Cassim says these actions play a valuable purpose in the market.

"By creating a credible or realistic prospect of appraisal, companies are encouraged to offer a fair price at the very outset to minimise the risk of appraisal arbitrageurs accumulating the company's shares and seeking appraisal."

In other words, while outraged executives tend to paint Cilliers and his distressingly few activist colleagues as "opportunists", the reality is this "appraisal rights" mechanism discourages opportunism by these very executives.