

# THE EVOLUTION OF CLASS ACTIONS IN SOUTH AFRICA

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Legal Briefings - By **Jonathan Ripley-Evans and Fiorella Noriega Del Valle**

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Unlike development driven by legislative reform, the evolution of the common law through the process of judicial precedent takes time. Here, development only occurs when the courts are seized with a case worthy of an evolutionary push and this means that, even when deficiencies in the law are self-evident, one has to wait for the judiciary to address the issue.

The law surrounding class actions in South Africa has not had the benefit of a legislative punt which would have sped up the process of legal development. It is therefore no surprise that any new (potential) class action raises excitement at the prospect of developing new law.

Against that background, the South African High Court's recent decision refusing to certify a shareholder class action against a company's directors, in the case of *De Bruyn v Steinhoff International Holdings N.V. and Others* ("Steinhoff"), is of great interest – particularly in illustrating the significant hurdles involved.

## CERTIFICATION

South Africa is no *old hand* at class actions, with the earliest cases emerging as recently as the mid-nineties. Since then the courts have only adjudicated on a handful of cases, the majority of which never made it past the certification stage.

Certification is the first hurdle which any enthusiastic class of claimants has to overcome, obtaining the court's stamp of approval to speak from one mouth. Only once the court is satisfied that the certification of a class is appropriate, will the matter move on to the more substantive aspects of the dispute. However, as was seen in *Steinhoff*, the merits of a particular claim do play an important role, even as early as at the certification stage of proceedings.

The party applying for certification usually attaches a draft particulars of claim and draft notice of class action in respect of the proposed action to be brought. The application is required to deal with the following factors:

- a. The existence of an objectively identified class of claimants;
- b. The suitability of a proposed class representative;
- c. The existence of a valid cause of action, which raises a triable issue;
- d. The issue/s to be determined must be common to all members of the class;
- e. The relief sought must flow from the cause of action and must be ascertainable and capable of determination;
- f. If damages are claimed, there must be a procedure by which damages can be allocated to members of the class which is appropriate given the composition of the class and the nature of the proposed action; and
- g. The class action must be the most appropriate means by which the claims of the class may be determined.

These factors are not necessarily exhaustive, nor are they prerequisites for the certification of a class. They are simply considerations which must be considered and weighed against the interests of justice.

In addition, the applicants are expected to provide details of how the class is to be notified of the proposed action and whether it is proposed as an opt in or opt out action.

## **SHAREHOLDER CLASS ACTIONS**

Although common in other jurisdictions, "shareholder" class actions had never been seen in South Africa – that was until *Steinhoff*. This decision has clarified important aspects of the certification function of the courts as well as the potential for shareholders to bring claims against directors for negligence.

On 5 December 2017, Steinhoff NV issued a press release, disclosing that information had come to light concerning accounting irregularities in the company. Thereafter, Steinhoff NV's share price fell by almost 96%. Shareholders who lost the greater part of their investment then approached the South African courts for relief.

The Steinhoff decision concerns the first stage of the class action procedure - an application for the certification of a class of shareholders of Steinhoff NV, who intend instituting a class action against Steinhoff, its directors and its auditors, in an effort to recover their losses.

In deciding whether to certify the class, the court considered the abovementioned factors in relation to class actions. Whilst the requirement that the would-be claimants demonstrate a valid cause of action which raises a triable issue appears, on the face of it, relatively simple, the court mulled over the scenario where a court is faced, at the certification stage, with a cause of action which relies upon a new point of law.

The court held that in such a case, it should, as early as the certification stage, decide the particular question of law for itself (insofar as it is able to do so), in an effort to determine whether there are in fact triable issues that warrant the certification of a class action.

Turning to the facts at hand, the Steinhoff shareholders alleged that -

- a. Steinhoff, through its directors, made negligent misstatements concerning Steinhoff. In particular, they overstated the assets, income and profits and understated the liabilities and expenses in circumstances where they were required to disclose the true position in Steinhoff's financial statements, for the benefit of existing and potential shareholders.
- b. Their conduct led to the Steinhoff shares being traded at inflated levels and the shareholders were unable to appreciate the true financial state of affairs and solvency. When the falsity of the misstatements was made public, the shares suffered a dramatic fall which caused loss to the shareholders.
- c. Steinhoff and its directors owed the shareholders a duty of care, both at common law and in terms of legislation. Steinhoff, through its directors, failed to carry out their duties which caused the shareholders to suffer loss.

In response, the directors argued that the shareholders had failed to show that they had a valid cause of action, and further that there was no triable issue. The court was therefore forced to determine whether a valid cause of action and the presence of a triable issue had been established.

# THE STEINHOFF DECISION

It is a long established principle of South African law that causing pure economic loss is not, in itself, actionable. In order to show that the conduct is actionable, the aggrieved party must show that they have a right or a legally recognised interest that has been infringed. As the claim by the shareholders fell within the four corners of “pure economic loss”, the court had to determine whether there was a right or legally recognised interest which had been infringed by the Steinhoff directors.

It is another well-established principle of South African law that the directors of a company owe a fiduciary duty toward the company, and not to the shareholders directly (in the absence of a special, factual relationship between the directors and shareholders which, the court found, did not exist).

The court found there was no reason to depart from this principle of the common law for a number of reasons. The most important of those reasons is that the company itself may have a claim for damages against the directors (given the duty owed by directors to the company), which would ultimately benefit the shareholders. As such, the shareholders must rely on the company to claim for any of its losses and thereby ultimately share in any recovery. Allowing otherwise may permit the duplication of claims.

The court also found that establishing a direct liability of directors toward shareholders, particularly in listed entities, would deter many candidates from accepting appointments to the board. Furthermore, the court considered the fact that the shareholders are able to enjoy the benefits of a limited liability company (which is limited only to the extent of their capital investment) and found that there is no need to give such shareholders the ability to look to the directors of a company in order to underpin the value of their shares.

Although the court recognised the severity of the losses and expressed sympathy for the shareholders, particularly as most of the considerations for the certification of a class had been satisfied, it was ultimately not able to certify the class due to the lack of a cause of action raising a triable issue.

## CONCLUSION

This judgment comes at an important time with the number of speculative claims being launched by prospective litigants on the rise. Often with such claims, the disputes are settled shortly after the certification of a class without ever reaching trial. This judgment has the potential to reduce the number of speculative claims launched with the primary aim of extracting settlement.

[More on Class Actions](#)

## KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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