THE POWERS OF DIRECTORS AND LIMITATIONS

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Table of Contents

Chapter 1

INTRODUCTION

The introduction of the new Companies Act has brought about sweeping changes within the field of Company Law.[1] Some of the most important changes relate to the duties of directors. The purpose of this dissertation is to investigate the exact extent and nature of the powers and duties of directors contained within specifically sections 66(1) and 76.

Chapter 2: The Source of Director's Powers

This chapter deals with the source of the powers of directors. Section 66(1) is the general empowering authority for directors to act and bind the company. Since most of the day-to-day actions of directors are valid by virtue of this section, it forms the foundational cornerstone of director's duties. This chapter goes into the detail on the exact nature of this power and expounds exactly on what this power entails.

Chapter 3: Statutory Limitation on Director's Powers

While S66 deals with the authority to conduct the business of the company, S76 gives the measuring staff against which the actions of directors must be measured. Stated differently, it provides a tool for determining whether a director's actions are acceptable for a person in such a position of authority. Essentially, it is a method of curtailing the incredibly wide powers given to directors in S66.

S76(1) defines who the individuals are who must comply with the standard of conduct expected of directors. Information gained by an individual by virtue of being a director is discussed in S76(2) as well as when such information may be used by that person for their own benefit. Subsection (3) deals with the duty of care and skill expected from the director. This duty of care and skill is further qualified by S76(4), which gives, *inter alia*, a concrete test for measuring if the director has met the minimum standard of conduct expected. It further provides a safe-harbor for directors who would have failed the test due to the fact that they either delegated authority to or relied upon information from a person defined in S76(5), which includes employees and legal council.

1 The Companies Act 71 of 2008 (The Act hereafter). Any reference to a section will be deemed to refer to the Act unless specifically stated otherwise.

Chapter 4: Common Law Limitations on Director's Powers

Since the common law has not been specifically excluded, it remains fully in force.[2] This chapter will briefly detail some of the major common law limitations on the powers of directors. Because there is already a large library of work on this topic, it will remain very brief.

Chapter 5: Conclusion

In this chapter, the information contained in the other chapters will be summarized briefly.

Limitations:

This dissertation will focus on the 2008 Companies Act as well as the common law on the selected sections. Any information, rulings and legislation outside the above will not be discussed. Where outside information has been brought in, it will only be discussed in light of the focus of this dissertation.

2 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 298 *et seq*.

CHAPTER 2

THE SOURCE OF A DIRECTORS' POWERS

Introduction

A body corporate cannot act on its own. Since it is an artificial entity, it must act through the people associated with it, whether they are employees, shareholders, directors or agents[3]. These individuals, when properly authorized, are not merely representatives or agents but act as the embodiment of the company itself.[4] However, while a company can interact with the outside world through any of these individuals, it is the directors who dictate how the company interacts. Because a company, and by implication its legal personality, is created by legislation and registration, all of its powers and authority originate from those documents. Consequently, the directors, as the primary shapers of the will of the company, must find their power and authority in the same sources as the company itself. In this chapter, one of the most important empowering provisions of directors will be discussed.

While the bulk of this dissertation will focus on the duties and limitations placed upon directors, section 66 still remains the basis of the discussion. It is illogical to discuss limitations placed on a power without at the very least defining it. That is the purpose of this chapter: to discuss section 66 in depth as the empowering provision so that the discussion on limitations may be more meaningful.

Source of the Director's Powers

"Section 66. Board, directors and prescribed officers.

(1) The business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that this Act or the company's Memorandum of Incorporation provides otherwise."[5]

Although comparatively short, section 66 is perhaps one of the most important sections in the entire Act. Despite its diminutive appearance, it effectively forms the central nervous system of a

3 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 255.
4 Tesco Supermarket Ltd v Nattrass 1971 2 All ER 127 (HL) at p170.
5 S66.

company. In simple terms, this section grants directors the authority to make decisions for the company. While this is sufficient for explaining the section to a lay person, the legal practitioner and directors would do well to become more informed of the consequences and implications of this content-rich section. In legal terminology, section 66(1) is the empowering legislation which grants directors the authority to manage the company in any manner which they see fit subject to certain restrictions. Some of these restrictions will be discussed in the subsequent chapters of this dissertation. It is still unclear whether section 66(1) places a positive obligation on directors to manage the company or merely regulates the relationship between directors and shareholders.[6]

Section 66(1) states that the directors must 'manage' the business and affairs of the company. Henochsberg concludes that 'manage' enables directors to act in any manner of management including all aspects of the business and even its winding up.[7]

The term 'business and affairs' of a company further radically empowers a company's directors and alters major aspects of company law as it stood in the previous Act. It should be noted that the power to manage the business and affairs is now an original power and is no longer delegated to the board from the shareholders.[8] Section 66(1) gives directors power over the 'business and affairs' of the company. As such, the definition of 'business and affairs' forms the cornerstone of the powers of the board of directors. Unfortunately, the Act does not define the term 'business and affairs'. The definition must therefore be determined by looking at case law, older legislation and provisions within the Act itself.

The *locus classicus* for the definition of 'business and affairs' comes from *Ex parte Russlyn Construction (Pty) Ltd*.[9] The case itself deals with the winding up of a business and whether the directors have the authority to do so. It should be noted that despite case being decided under the 1973 Act, it is submitted that it remains relevant here. In the case, it states 'affairs' as being a concept wider than 'business'.[10] While not a definition *per se*, it is an important qualification since it serves as proof that, in the very least, 'business' and 'affairs' are two distinct concepts which may overlap.

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6 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 247.
7 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 248 read with *Ex party Russlyn Construction (Pty) Ltd* 1987 (1) SA 33 (D).
8 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p. 248
9 1987 (1) SA 33 (D)
10 See generally *Ex parte* Russlyn Construction (Pty) Ltd 1987 (1) SA 33 (D) 36-37

The 1973 Act also does not define 'business or affairs' directly. It does, however, define place of business. This will be discussed below.

Henochsberg submits that the conclusion that 'affairs' is wider than 'business' as defined in *ex parte Russlyn* is correct.[11] Delport states that 'business' refers to dealings between the company and outsiders and that 'affairs' is a wider concept which refers to both the internal relations of a company and its existence.[12] For further clarity, it may be wise to compare it to the Canadian Business Corporation Act.[13] Like South Africa, Canada has a supreme constitution and it is a country that used to be a British Colony. In addition, the South African Companies Act is based largely upon the Canadian one. In the Canadian Business Corporation Act it states that 'affairs' means "the relationship 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 ('*affaires internes'*)".[14] It should be noted that in the French version of their Business Corporation Act, it specifically refers to '*affaires internes*' or internal affairs while our Act only refers to the term 'affairs'. Therefore, it may be possible that the Canadian definition of affairs and the definition of affairs in the South African Companies Act are substantively different. It is submitted that the definition of affairs within the Act is wider than the Canadian '*affaires internes*'.

In support of the above, the following is submitted. Although not directly defined in the Act, the meaning of 'affairs' can be inferred from its usage throughout the Act. In its definition of 'accounting records', the Act refers to financial affairs and states that it includes "purchase and sales records, general and subsidiary ledgers and other documents and books used in the preparation of financial statements".[15] Section 82(1) orders the Master to file a certificate of winding up of a company once the affairs of the company have been completely wound up. In such a situation envisioned by section 82(1), the company no longer has any influence upon the outside world or any outstanding matters left to deal with. In other words, it is wound up and no longer has any open affairs. The definition of 'business rescue' also references affairs alongside business, property, debt and other liabilities.[16] If one can assume that words are not tautologically placed by the legislature,

11 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 248.
12 The New Companies Act Manual Including Close Corporations and Partnerships (Student Edition), P. Delport, Lexis Nexis, 2011, p66.
13 R.S.O. 1990, Chapter B. 16.
14 S2(1) of the Business Corporation Act R.S.O. 1990, Chapter B.16.
15 S1 of the Companies Act 71 of 2008.
16 S128(1)(b) of the Companies Act 71 of 2008.

it is again submitted 'affairs' has a separate meaning from 'business'. 'Affairs' therefore does not mean property, debts or other liabilities. By this same logic, 'affairs' also has a separate meaning from the financial situation of the company.[17] In addition, affairs can have books and records relating to them.[18] Section 142 gives perhaps the best insight into what 'affairs' is comprised of. Before business rescue may be affected, the director must provide a statement of affairs which must contain at the minimum:

(a) Any material transaction involving the assets of the company.
(b) Any court, arbitration or administrative proceedings involving the company.
(c) The assets and liabilities of the company, as well as its income and disbursements.
(d) Any debtors and their obligations.
(e) Any creditors and their claims.[19]

However, since the legislature specifically use the word 'minimum', one may assume that definition of 'affairs' can be wider than (a) to (f) listed *supra*. Affairs can also be contained in the Memorandum of Incorporation and shareholders agreements.[20] By taking the above into account, it is submitted that the word 'affairs' refers to the day to day operation of the company and legal implications thereof, including contracts with creditors and debtors, matters involving the assets of the company, how liabilities are handled and any court proceedings. Essentially, 'affairs' refers to the internal relationships of a company, in addition to certain legal aspects related to carrying on business with the outside world.

If one assumes the above to be true, then the definition of 'business' must also be different to avoid tautology. Again, the term 'business' is not directly defined in the Act. The 1973 Act defines 'place of business' as "any place where the company transacts or holds itself out as transacting business and includes a share transfer or share registration office".[21] One may therefore infer that in terms of the 1973 Act business refers to an act which causes business transactions including the transfer of shares.

However, a functional definition may be deduced from section 8(3) of the Act. In terms of this section, 'business' means actions with the object of acquiring financial gain. But, since business and

17 S141(1) of the Companies Act 71 of 2008.
18 S142(1) of the Companies Act 71 of 2008.
19 S142(3)(a-f) of the Companies Act 71 of 2008 paraphrased.
20 S163 of the Companies Act 71 of 2008.
21 S1 of the Companies Act 61 of 1973.

affairs are specifically named, it can be assumed that they have different definitions, although some overlapping is possible. Business then must refer to all actions that are not 'affairs', that is, all actions not involving contracts, credit, purchasing and selling of assets *et cetera*. It is submitted that business then must refer to production, since affairs essentially refer to all matters surrounding production and as per the derived definition from the 1973 Act, it would also include the purchase and sale of its own shares. Therefore, business refers to the physical creation of the product or the rendering of the service and all matters dealing with this save those which fall within the ambit of affairs and also includes the sale of its own shares. This new definition still harmonizes with the definition stated by Delport *supra*. To illustrate, while the submitted definition of affairs deals with the consequences of a purchase and sale (e.g. the obligations owed to creditors or by debtors), it does not deal with the purchase or sale itself. Therefore, 'business' can be seen as the relationship between the company and the outside world, save for those elements which fall under the domain of 'affairs'.

In summary, it is submitted that 'business' refers to the physical acts of production, rendering of services, purchase and sale, while 'affairs' deals with matters surrounding 'business' such as the conclusion of contracts, the provision of credit and the handling of court cases. However, 'affairs' may also include aspects of 'business' as per the findings in *ex parte Russlyn Corporation (Pty) Ltd*.

Regardless of the exact meaning of 'business and affairs', the fact that section 66 placed authority over business and affairs squarely in the hands of directors implies, as Delport states, that the ultimate decision making power now rests with the board and not with the shareholders, save where the memorandum of incorporation or Act provides otherwise.[22] Henochsberg also refers to it as the ultimate power in the company and, provided section 66 is complied with, the board of directors is the ultimate organ of the company.[23]

The section continues by stating the business and affairs of a company must be managed 'by or *under the direction* of the board'.[24] This implies that directors may delegate certain aspects of their authority. The Act recognizes the practical elements of running a business. It might not always be possible or wise for directors to perform each and every duty themselves, especially when making a

22 The New Companies Act Manual Including Close Corporations and Partnerships (Student Edition), P. Delport, Lexis Nexis, 2011, p67.
23 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p. 248 and 249.
24 S66(1).

certain decision or performing a particular duty requires special knowledge or large quantities of research which a director does not have time or skills to engage in properly. This statement is further supported by section 72 which gives directors the power to appoint committees.

Section 66(1) continues by stating that directors may exercise all the powers of the company and perform any of its functions. This shows once more the extent of the powers directors have at their disposal. It is submitted that this section's most important implication is that it directly empowers directors to bind the company. This is so because the director can, *inter alia*, perform the functions of the company. It can be stated that one of the functions of the company is to engage in business transactions. This naturally entails entering into contracts with third parties and section 66 therefore empowers directors to contractually bind the company. This also further empowers directors to engage and participate in legal proceedings as long as the director is properly authorized to do so by the board.[25]

Just as section 66 establishes the power of directors, it also lays the foundation upon which legislative limitations are placed. The section ends by stating that directors have wide sweeping powers *subject* to the Act or memorandum of incorporation. Firstly, this entails that the memorandum can limit any powers of any director. This further implies that the management of a company can be tailored to the specific needs of a company. However, it is unclear whether the memorandum can be drafted in such a manner as to exclude all of the powers of a director.[26] Secondly, it forms the framework for the restrictions on that power in section 76 as it states that these powers may be limited by legislation. Naturally, the common law and its limitations on the authority and powers of directors still apply since it is not specifically excluded.[27]

25 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 249 *et seq*.
26 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p.247.
27 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 298 *et seq*.

CHAPTER 3

STATUTORY LIMITATION ON A DIRECTOR'S POWERS IN SECTION 76

Introduction

From the previous chapter, it is clear that directors have wide, sweeping powers to manage a company. Such power cannot go unregulated. Because of the fiduciary nature of the position of directors, they have control over the property of other individuals.[28] In most companies, this leaves shareholders vulnerable to the powers and discretion of the director.[29] Left uncontrolled, this allows unscrupulous individuals to misappropriate the property of the third party (shareholders *in casu*) and leave them without recourse. Naturally, this situation is untenable and *contra boni mores*. It is for this reason that strict and well-defined limitations must be placed upon a director's otherwise near-unlimited powers. These limitations are of such importance that it is imperative they continue to apply even after a director has resigned.[30] In this chapter, the legislative limitations placed upon directors will be examined as they are contained in section 76. This section contains multiple provisions regarding handling of important information, the conduct expected of directors and their fiduciary duties.

Origins

The powers granted by section 66 can be limited by the Act or a Memorandum of Incorporation.[31] Also, because the Act does not specifically exclude it, the common law still applies in so far as it is not in direct conflict with the Act.[32] Historically and legislatively, it is clear that there must be some standard against which a director's actions and conduct must be measured. This measure originates from the fiduciary relationship between the company and directors, and the duties which flow from that relationship. These duties can be generally summarised as requiring the director to act with the

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28 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 509.
29 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 512.
30 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p547.
31 S66(1).
32 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 287.

character traits of good faith, honesty and loyalty.[33] Although not fiduciary duties, a director also has the duty to exercise care and skill.[34] The basic rule can be summarized in that as long as a director acts honestly, he or she cannot be made responsible in damages unless guilty of gross negligence.[35] However, abstract concepts often do not make for clear rules. As such, the common law and legislation have fleshed out those attributes into a series of largely clear standards and tests. Furthermore, these duties are mandatory, prescriptive and unalterable and they apply to all companies.[36] The purpose of these duties is to raise the standards of corporate and directorial behavior as well as serve as a deterrent against abuse of power by directors.[37]

From a fundamental standpoint, a director is held responsible for his actions because he is a fiduciary. A fiduciary is someone who has the discretion and power to act unilaterally in order to influence the matters of another and that third party is “at the mercy of the fiduciary”.[38] Despite similarities, a director isn't a mere trustee.[39] In *Cohen v Segal* it was held that the director owes his fiduciary duties to the company and not to anyone else.[40] In other words, a director owes no fiduciary duties to an individual shareholder even where that individual shareholder is the majority shareholder.[41] A director’s fundamental duty is to act in the best interests of the company.[42] The shareholders in their personal capacity are not owed a duty directly but they are still protected since as the body of the company.[43]

While the origin of the majority of the fiduciary duties of a director stem from common law, the Act has partially codified them,[44] meaning only part of the common law has been set out in legislation. This naturally entails that both the common law and the legislation operate in tandem. Put differently, while the Act does codify a part of the fiduciary duties into section 76, “it is not a comprehensive or fully self-contained code of fiduciary duties”.[45] Cassim states that partial codification can be both good and bad. The advantages are that this makes the law more clear and

33 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 507.
34 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 507.
35 In re Brazilian Rubber Plantation and Estates Ltd [1911] 1 Ch 425 at [436].
36 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 507.
37 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 507.
38 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 513.
39 Fergison v Wilson (1866) 2 Ch App 77; 15 LT 230 at [89] read with Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 513.
40 1970 (3) SA 702 (W) 706.
41 Bell v Lever Brothers Ltd (1932) AC 161 (HL) at 228 read with Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(1).
42 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(3).
43 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(3).
44 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 507.
45 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 507.

accessible, but may stifle the flexibility and development of these duties.[46] It is argued that the fiduciary duties should always be given room to develop and that they should never become static.[47] Fortunately, the Act avoids the stagnation of growth by not excluding the common law duties and, in essence, requiring a director to meet both the common law and statutory standards.[48] As an illustration, this means that in the event where a director complies with the requirements of the Act, but his actions are still so reprehensible that a court cannot abide them, a judge still retains the authority to develop the common law to halt such behavior without being forced to involve the legislature and the often lengthy procedures to alter or amend legislation.

Definition of a Director

While it is clear why there must be a limitation on a director's authority, it is important to know to whom exactly these limitations apply. Section 1 defines a director as "a member of the board of the company, as contemplated in section 66, or an alternate director of a company and includes any person occupying the position of a director or alternate director, by whatever name designated". Paraphrased, section 66(1) states that a director is a natural person who manages the business and affairs of a company. Note that the definition of director contained in section 1 has been widened to include a person exercising a director's authority even where he is not designated as such. This means that where a person who is not a director, but who still dictates the operation of a company as a director would, still falls within the ambit of the section 1 definition. His actions will be measured against the same standards as other directors and he will incur the same liabilities as a director would. That non-director would therefore be deemed a director in all but name. Such a non-traditional director is known as a *de facto* director.[49] The widened definition also makes fiduciary duties applicable to so called shadow directors or puppet master directors. These are individuals who are not appointed by the company, but who still influence or manipulate the board "from the shadows".[50] Hiemstra J in *S v Shaban* even went as far as to say, "I want to destroy any idea that puppets can be lawfully employed in our company system" and found a shadow director *in casu* guilty of fraud.[51] Although the Act has been largely decriminalized, it remains improper and carries serious consequences.

46 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 507-508.
47 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 507.
48 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 508.
49 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 508.
50 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 508.
51 S v Shaban 1965 (4) SA 646 (W) at [651].

Section 76 has made the definition of a director even wider:

76. Standards of directors conduct.

(1) In this section, "director" includes an alternate director, and—

(*a*) a prescribed officer; or

(*b*) a person who is a member of a committee of a board of a company, or of the audit committee of a company, irrespective of whether or not the person is also a member of the company's board.

Section 1 defines a prescribed officer as a "person who, within a company, performs any function that has been designated by the Minister in terms of section 66(10)". In addition to section 76(1)(b), section 72(2) states that a committee of the board may include a person who is not a director. Because of how wide the application of the above sections stretches, it is important for any individual acting in a company to be certain of whether the standard of conduct expected of directors is applicable to him or her, lest they become liable for not meeting the requirements expected of a director. Cassim states that everyone from an *ex officio* director to senior employees or senior management and even prescribed officers, members of the audit committee or board committees (regardless of the fact that they do not have a vote on the board of directors) may be deemed to be a director in terms of the Act under the right circumstances.[52]

Limitation on the Use of Information

As established, directors have wide powers and control the company. Logically, in order to exercise those powers effectively, directors must be well informed of the status the company and any matters surrounding its operations. This information has become one of a company's most valuable assets and as such should be properly protected, especially from unscrupulous directors who would use it for personal profit.[53] As an example, suppose that a company would report to the public that it would be liquidated within a week. This would cause share prices to drop significantly. A director in possession of this information might be able to sell his shares the day before the liquidation announcement and thereby avoid personal loss. Another example would be where a director uses information about an upcoming business opportunity to undercut the company.

Section 76(2) was implemented to prevent situations similar to the ones mentioned above. In the most basic terms, section 76(2) prohibits a director from using information gained by virtue of his office for personal gain. Subsection (2)(a) reads as follows:

52 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 508-509.
53 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 554.

(2) A director of a company must—

(*a*) not use the position of director, or any information obtained while acting in the capacity of a director—

(i) to gain an advantage for the director, or for another person other than the company or a wholly-owned subsidiary of the company; or

(ii) to knowingly cause harm to the company or a subsidiary of the company

Again, the departure point must be how wide the net of limitation is cast. Firstly, information gained as a director may not be used to the benefit of the director himself. Second follows the catch-all phrase, namely, such information must be to the benefit of the company or a wholly owned subsidiary only. It amounts to a form of exception. A director may use information gained to benefit a wholly-owned subsidiary instead of the principle company. Cassim states that for this section to be applicable, the following requirements must be met:

- The defendant must be a director within the definition of a director contained in section 76.
- The information or advantage must have come to the director.
- The director must have used his/her position as or information gained as a result of being a director to gain an advantage or knowingly cause harm to the company or wholly owned subsidiary.
- Such advantage (where applicable), must have been obtained for the director or some other person other than the company or wholly owned subsidiary.[54]

In other words, a director is prohibited from using any information gained from being director for any other person save the company and its wholly-owned subsidiary. A wholly owned subsidiary is defined as another juristic person in which the company holds or controls all of the voting rights.[55] Such control may be in the form of holding the majority of shares or having the ability to elect the appointment of directors or any combination thereof.[56] In such a case, the wholly-owned subsidiary is essentially a puppet of the holding company and can be seen as an extension of the holding company. This also implies that a director would fail in his fiduciary duty where he used information to benefit a partially owned subsidiary.

At first glance it may appear that section 76(2)(a)(i) allows free communication of information between holding and wholly owned subsidiary companies. But what happens in a situation where a

54 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 552.
55 S3(1)(b).
56 S3(1)(a) read with S3(1)(b).

director may be in possession of information that may be used to the benefit of the wholly owned subsidiary, but which may be used to the detriment of the holding company? The section specifically relates to instances where the position or information may be used to "gain an advantage" as the result of sharing the information.[57] This section is framed in the positive and entails that the company suffering some detriment or being disadvantaged is not a requirement for the director to have failed in his duties.[58] The requirement in section 76(2)(a)(ii), instead, refers to "knowingly cause harm" and places the emphasis on the subjective intention of the director. Regardless, section 76(3)(b) states a director must act in the best interest of the company. Note that this section makes no reference to any subsidiary and is therefore only limited to the company employing the director. In other words, the director's fiduciary duties are only in respect of his own company. Therefore, section 76(2)(a)(i) would allow a director to share information with a wholly-owned subsidiary to the detriment of the holding company, but doing so would be a breach of the fiduciary duties owed to the holding company. Therefore, it is submitted when dealing with information sharing between a holding company and its wholly-owned subsidiary, there must be no detriment to the holding company by the sharing of the information lest the director sharing the information be found liable for breach of his fiduciary duties.

However, this section creates another anomaly in company law. As stated, a director's fiduciary duties are limited only to the company which employs him.[59] Furthermore, at common law a director does not owe a fiduciary duty to a subsidiary company.[60] However, section 76(2)(a)(ii) states that a director may not use any information gained from being a director to knowingly harm the company or a wholly owned subsidiary. 'Knowingly' is defined in section 1 as where a person, in relation to a particular matter—

- Has actual knowledge; or
- Was in a position in which a person reasonably ought to have had actual knowledge, investigated the matter to the extent that would have provided the person with actual knowledge or taken other measures which, if taken, would reasonably be expected to have provided the person with actual knowledge of the matter.[61]

From the above definition it is clear that 'knowingly' refers to an objective determination and

57 S76(2)(1)(i).
58 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 550.
59 S76(3)(b).
60 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 551.
61 S1.

Cassim states that the test would lose much of its effectiveness if the courts applied it subjectively.[62] With this in mind, it means that a director now has a limited fiduciary duty towards the wholly owned subsidiary which he didn't have before. This may become problematic in practice. For example, a holding company may wish to affect a triangle take-over, the goal of which is to secure a greater market share. In other words, the holding company will use the wholly owned subsidiary company to take over a third company. This is done to limit the risk and potential loss of the holding company. For purposes of this example, we may assume that all regulations in terms of take-over and competition law are fully complied with. After doing their due diligence, the directors determine that because of its internal problems of the third company, the share price of the wholly owned subsidiary will drop and it will suffer a significant loss, but because of the increased market share, the holding company stands to make a large profit. However, the operation of section 76(2)(a)(ii) means that the directors who used information obtained by virtue of being a director and caused harm to a wholly owned subsidiary can be held liable for a breach of fiduciary duties.

Cassim correctly states that S76(2)(a) may be unnecessarily wide and excessive.[63] However, the practical impact of this may be less significant. Section 77(2) states that a director *may* be held liable for a breach in terms of section 76(2).[64] In other words, the aggrieved party (the wholly-owned subsidiary *in casu*) may elect to hold the directors liable for the loss they have suffered. However, since the wholly-owned company is held by the principle company, the directors would then in fact institute action against themselves. Obviously, a board of directors will not do so within the ordinary scope of business. Nevertheless, this does not mean that the above scenario will never occur. It is submitted that in certain instances, a board may use this as a mechanism to rid itself of a member of the board, the legality of which falls outside the ambit of this dissertation. However, this position may be different with a partially owned subsidiary.

Since section 76(2)(a) prohibits that the director uses such information for the benefit of any person other than the company, it implies therefore that he must use this information to benefit the company. The question now is whether there a limitation on this duty. Henochsberg states that a director has a duty to acquire some corporate opportunities for a company which he frames as either property, rights or information.[65] Should a director gain such a corporate opportunity for himself,

62 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 552.
63 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 551.
64 Emphasis added.
65 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 289 and 290.

the law will treat the acquisition as being made on behalf of the company.[66] He may also be liable for breach of his fiduciary duties in terms of section 77. However, it would be unimaginable for all acquisitions made by a director to be subject to a blanket claim by the company on pain of personal liability. To illustrate, a director may purchase a plot of land so that he may build his house on it. Further suppose that the company which employs him is in the business of property development. Should the blanket claim apply, the director may be prevented from ever purchasing any property or face severe consequences should he ever do so. This situation is obviously untenable and the courts seem to agree. It has been held that a director is not obliged to offer all property developments of whatever nature to the company, save where there has been an agreement to that effect.[67] It is submitted that the term 'property developments' can be substituted with any 'corporate opportunity' as required by context and the ruling will still remain valid. It was also held that it would be intolerable if a director were held accountable for every private purchase the company might want to conclude.[68] It is impossible and unwise to formulate a general rule for determining when a corporate opportunity may be appropriated by a director and every case must be judged on its own merits.[69] Professor Havenga states that the test which is applicable in South Africa has two steps:

- The corporate opportunity must be in line with the business of the company and
- Under the circumstances, the company has to justifiably rely upon the director to acquire or assist in the acquisition of the corporate opportunity.[70]

This was quoted with approval in the *Movie Camera Corporation* case.[71]

Henochsberg seems to imply that this section also places a duty upon the director to account for secret profits. In the *Robinson* case, it was held that "the term 'profits' is a wide one, especially when used in connection with accountability for breach of fiduciary duties".[72] Innes CJ continues, "It is not confined to money, but covers every gain or advantage made by a wrongdoer".[73] A director's liability to account is linked to the fact that profit has been made and not to the presence of any form of fraud or the absence of *bona fides*.[74]

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66 African Claim and Land Co Ltd v Langermann 1905 TS 494 at 505 and Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p289.
67 Ghersi v Tiber Developments (Pty) Ltd 2007 (4) SA 536 (SCA) at para 9.
68 Robinson v Randfontein Estates Gold Mining Co Ltd 1921 AD 168 at 268.
69 Movie Camera Company (Pty) Ltd v Van Wyk and Another (2003) 2 All SA 291 (C) at para 48.
70 Corporate Opportunities: South African Update, M Havenga, SA Merc LJ 1996 (8) 40 at p46.
71 Movie Camera Company (Pty) Ltd v Van Wyk and Another (2003) 2 All SA 291 (C) at para 45 and 57.
72 Robinson v Randfontein Estates Gold Mining Co Ltd 1921 AD 168 at 159.
73 Robinson v Randfontein Estates Gold Mining Co Ltd 1921 AD 168 at 159.
74 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 291.

Section 76(2)(b) provides a safe harbour for directors. As long as they comply with the requirements of this section, they cannot be held liable for breach of their information duties.

Section 76(2)(b):

(*b*) communicate to the board at the earliest practicable opportunity any information that comes to the director's attention, unless the director—

(i) reasonably believes that the information is—

(*aa*) immaterial to the company; or

(*bb*) generally available to the public, or known to the other directors; or

(ii) is bound not to disclose that information by a legal or ethical obligation ofconfidentiality.

Section 76(2)(b) only comes into effect once a director has breached his information duties. Should he be able to comply with this section, he will avoid any personal financial liability for any loss or damage caused by his breach. However, where the requirements for the founding of liability is relatively wide, the exemption against it is very narrow and specific.

The source of the information obtained while acting as a director is irrelevant.[75] Therefore, it is does not matter whether the director had become aware of in his personal or professional capacity.[76]

The section details specific steps which should be taken in order to avoid personal liability. A director must communicate to the board at the "earliest possible opportunity" that he is in breach.[77] The question now is what 'communicate' means. Does such a communication have to be in person at a board meeting or will an e-mail or electronic memo be sufficient?

Within the Companies Act itself, 'communicate' isn't defined. It is, however, used in a few instances. It is used in section 63(2) where it allows shareholders to attend and participate at shareholders meetings via electronic communication technology should the memorandum of incorporation permit it. A similar provision is found in section 73(3) where board meetings could be held by means of electronic communications unless prohibited by the memorandum of incorporation or the Act. So at the very least, unless prohibited by the Memorandum or Act, it is possible that such a communication may be done electronically by means of a real time electronic communication system. The Electronic Communications and Transmission Act 25 of 2002 (ECTA

75 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 295.
76 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 295.
77 S76(2)(b).

hereafter) states that “information is not without legal force and effect merely on the grounds that it is wholly or partially in the form of a data message”.[78] It continues by saying that if there is a requirement by law that something must be in writing, the fact that such writing is in the form of a data message meets the requirement and therefore is deemed to be in writing.[79] A data message is defined as “data generated, sent received or stored by electronic means”.[80] It is submitted that such communication may be done either verbally at a board meeting or in the form of a document sent to the board members, unless the memorandum of incorporation or Act states otherwise. Where it is not prohibited in the memorandum of incorporation, such communication may be made by means of a voice-over Internet protocol (VOIP) program as long as it meets the requirements set out in section 73(3). In cases where written submissions are acceptable, an electronic message will be deemed to be equally acceptable.

The remaining part of section 76(2) expands upon which information a director need not share with the company and may not be held liable for not communicating.

Section 76(2)(b)(i) gives a test against which non-communication can be measured. A director must reasonably believe that the information is either immaterial, already within public knowledge or already known to the other directors. This is an objective test to the subjective knowledge of the non-communicating director. However, the Act is not clear as to whether the actions of the non-communication director must be measured against a reasonable person or against a reasonable director. Depending on the situation, the former may end up being a much lower standard to be measured against than the latter.

In other words, in establishing liability, it must be shown that a reasonable director in the position of the non-communicating director would have come to the same conclusions regarding both the nature of the information and that the communication would not have been necessary.

Section 76(2)(b)(i)(aa) states that a director need not communicate the information if it is immaterial to the company. This subsection has two primary purposes. Firstly, it protects the director and sets the limits of what must be disclosed. For example, a director need not disclose to the company that he will be getting a divorce, since it is immaterial to the company. Secondly, it

78 S11(1) of ECTA.
79 S12 of ECTA.
80 S1 of ECTA.

eliminates unnecessary communications to the board. Should this section not have been in place, irrelevant communications may have mistakenly made their way into board meetings and made the board more inefficient than necessary.

Subsection (bb) gives two further grounds attempting to improve the efficiency of the board. Firstly, if the information is already public knowledge, the directors are deemed to be aware of it. Secondly, if the directors are already aware of the information, it serves little purpose to have a director communicate it again. However, this section does not prevent a director from making such a communication. A director may feel the need to draw particular attention to the matter or he might require an official response from the board on the matter.

The final subsection protects the director from liability where he is incapable of communicating such information without breaching another legal or ethical obligation.[81] Legal obligations refer to obligations incurred either from a confidentiality agreement, for example one between an attorney and client, a non-disclosure agreement or an obligation originating from a court order. As to what an ethical obligation refers to is less clear. The term “ethical obligations” is only used once in the entire Act, namely in the above subsection. It is submitted that this refers to the case where a director is also either a doctor, a religious priest or where another form of professional privilege which is not attorney client privilege comes into being. To illustrate, confessions to a priest or anything revealed to a doctor by a patient enjoy some confidentiality but not to the extent where a court of law cannot inquire about it.[82] In other words, it gives rise to an ethical obligation of confidentiality, but not a legally enforceable one. It remains to be seen which ethical obligations exactly will qualify in terms of this section.

Limitations of the Power and Authority of Directors

Section 76(3) is the core of a director's duty towards the company. It contains the good faith requirements as well as the duties of care and skill. It essentially gives us the general tests for when a director's conduct is permissible. The primary consequence of section 76(3) is that if a director does not pass the tests set out in the section, he can be held liable personally liable for any loss or damage suffered by the company due to his actions.[83] However, it may be more serious than that. Suppose a director breaches one of his fiduciary duties. It may entirely be possible, depending upon

81 S76(2)(b)(ii).
82 Principles of Evidence 3rd Edition, P. Schwikkard, Juta, 2009, p152-153.
83 See generally S77 and specifically S77(2) and (3).

the circumstances, that this can amount to both a breach his duty of care and skill as well as the criminal offence of fraud or theft.[84]

Section 76(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; and

(*c*) with the degree of care, skill and diligence that may reasonably be expected of a person—

(i) carrying out the same functions in relation to the company as those carried out by that director; and

(ii) having the general knowledge, skill and experience of that director.

Before personal liability is founded, the director's actions are measured against the myriad of criteria listed in section 76(3). Should he fail to satisfy even one of the numerous criteria, he can be held personally liable in terms of section 77.

Subsection (3) starts off by qualifying itself subject to subsections (4) and (5), which will be discussed below. It then continues by stating that a director, when acting as a in his capacity as a director, must perform his functions in a specific manner. We have already discussed the extended definition of 'director' applicable under this section. However, subsection (3) specifically states that it comes into operation when a director acts as a director, thus limiting the situations where the section can be applied. For example, assume a company's memorandum of incorporation states that the company must have a 'social events planning committee' the purpose of which is to plan birthday celebrations for staff. It further states that a director must head this committee. Director B heads this committee, but does not fulfill his duties. In terms of section 76(3), he cannot be held liable, since planning birthday parties is not intrinsically part of being as a director and his failure to act was not as a director acting as director.

The section further limits its applicability to situations where the director must perform the powers and functions of directors. Powers and function of directors refers to any situation where a director must act. This includes where the director must act as empowered by section 66, act in board meetings, making distributions and issuing shares. This means subsection (3) only comes into effect in situations where a director must perform the function of a director. This entails that a director cannot be held liable in terms of this subsection for breach of his fiduciary duties should he, for

84 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296.

example, go onto the floor of his factory and work on the machinery, because that does not form part of the powers and functions of directors.

Subsection (3)(a) places the first and second qualifications on the powers of directors set out in section 66. It states that a director must use his powers in good faith and for proper purpose.

Good faith requires honesty.[85] Naturally, this entails a subjective knowledge of wrongdoing and therefore turns on the director's state of mind.[86] However, this is not an absolute rule. Where there is no reasonable ground for believing that the director is acting in the best interests of the company, it may be deemed that the director was not acting in good faith.[87] This is a subjective test.[88]

Cassim states that proper purpose and good faith are distinct yet cumulative.[89] Proper purpose would refer to only using the powers granted for the objective purpose for which they were intended and the test for this is objective.[90] It also entails that a director may not exceed the limitations of his own authority and must not exceed the capacity or authority of the company.[91] Essentially, a director may never use their powers to pursue an improper purpose.[92] To illustrate this principle, one may look at the issue of shares. This example is loosely based on the facts of *Hogg v Cramphorn Ltd*, but unlike that case, is framed in terms of the new Act.[93] The board is empowered to issue unissued and authorized shares.[94] The purpose of issuing shares is the generation of capital. This is partially supported by the emphasis and focus in section 40 on gaining adequate compensation or, in other words, issue shares in exchange for capital. Suppose a director wants to gain control of the majority of the voting rights of a company and issues unissued shares to his wife with board approval. Even if the director complies with all other requirements both within section 40 and all other applicable take-over requirements, it might still not be permissible because of the proper purpose requirement in section 76(3)(a). As established, the proper purpose of the issue of shares is the generation of capital and not for it to be mechanism for the manipulation of the control of a company. Therefore, the board may be held personally liable for breach of the duties contained

85 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 524.
86 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 524.
87 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 524.
88 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 526.
89 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 525.
90 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 525.
91 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(1).
92 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(1).
93 (1967) Ch 254.
94 S40(1).

in section 76(3). The fact that the directors honestly believed that acting outside their proper purpose duties was in the best interest of the company is irrelevant and they may still render themselves personally liable.[95] Cassim states that the appropriate test to determine whether this duty has been complied with is found in *Extrasure Travel Insurances Ltd v Scattergood*.[96] The four steps to this test are as follows:

- Identify the particular power being challenged.
- Identify the proper purpose for which the power was given.
- Identity the substantial purpose for which the power was in fact exercised.
- Decide whether the purpose was proper.[97]

It is important to note, once again, that fiduciary duties may attach to non-directors like prescribed officers or senior employees under certain circumstances.[98]

The third qualification placed on director is found in subsection (3)(b). It states that a director must act in the best interest of the company. “Of the company” in the context of section 76(3)(b) does not mean the company as the commercial entity. It refers to the collective body of present and future shareholders.[99] However, it may very well be that in order to act in the best interest of the company, the company may sometimes be required to pursue something more than pure profit. There are two schools of thought on this, namely the Pluralist Approach and the Enlightened Shareholder Approach.[100] The former entails that a company may sacrifice the needs of its shareholders in order to advance the interests of its stakeholders (e.g. employees or the community).[101] With the latter, the focus remains on profit as the ultimate goal, but permits directors to invest in stakeholders if it will ultimately result in a profit for the company long term.[102] In other words, the former allows a company to promote stakeholder's interest as an end *ipse*, rather than a means to an end as with the latter. Cassim states the following test found in *Charterbridge Corporation Ltd v Lloyd's Bank* should be used in order to determine whether a director has fulfilled his duty to act in the best interests of the company.[103] The test asks whether an intelligent and honest person in the position of the director could in the whole of the circumstance have reasonably believed that he or she was

95 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(1).
96 (2003) 1 BCLC (ChD) 619.
97 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 527-528.
98 Henochsberg on the Company Act 71 of 2008, Volume 1 Service Issue 2, Lexis Nexus, June 2012, p 296(4).
99 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 515 and Greenhalgh v Arderne Cinemas Ltd (1950) 2 ALL ER 1120 p1126E.
100 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 518.
101 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 518.
102 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 519.
103 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 525.

acting in the interest of the company.[104] This is an objective test.

With regards to who may claim from errand directors, it is interesting to note that classically, only the company could claim from directors and not individual shareholders, since the duties are fiduciaries of the company alone.[105] This has changed with the introduction of the section 164 derivative action which allows any interested party to institute action against a director. However, shareholders cannot claim for a loss in their share value from a director.[106] Cassim states this is because the loss in the value of the shares is merely a reflection of the loss suffered by the company and as such the shares were not directly affected by the actions of the director.[107]

The final qualification is a statutory version of the common law rule pertaining to care and skill. The care and skill test is comprised of objective and subjective elements. Subsection (3)(c) starts by giving the factors which must be compared, namely care, skill and diligence. The section implies that there is a difference between the terms ‘care’ and ‘diligence’.[108] ‘Skill’ means the technical competence of a director while care is the measure of how that competence or skill is applied.[109] ‘Diligence’ probably means attending properly to one’s duties.[110] Framed practically, this means devoting attention to company affairs, proper supervision and ongoing monitoring of company officers and employees and regularly attending board meetings.[111] There appears to be a shift that non-attendance of board meetings will eventually be seen as a failure to exercise reasonable care and diligence in the absence of a reasonable excuse.[112] In order to perform this test, the conduct of a director must be measured objectively and subjectively. This is known as a twofold, dual or hybrid standard.[113] Care refers to the objective element, while skill refers to the subjective element.[114] The objective portion of the test involves comparing the actions of a director with another director carrying out the same functions.[115] Cassim states that the director must be measured against a reasonable person and not a reasonable director.[116] Subjectively, a director must act in the same

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104 (1970) Ch 62 at 72 and Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 525.
105 Contemporary Conpany Law 2nd Edition, Cassim et al, Juta, 2012, p 516.
106 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 517.
107 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 517.
108 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 559.
109 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p556
110 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 560.
111 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 560.
112 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 560.
113 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 559.
114 Entrepreneurial Law Incorporating the New Companies Act (Special Edition); The New Companies Act Manual, ML Benade et al, Lexis Nexis, 2009, p135.
115 S76(3)(c)(i).
116 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 559.

manner as another director with the same knowledge, skill and experience.[117] This subsection entails that the more skilled a director, the higher the bar is to which he is compared and vice versa.[118] Experience, special skills or knowledge is not required of a director, so even an inexperienced director who made a costly mistake can find protection under this section as long as he complied with the minimum objective standards of reasonable care and skill.[119] It has been held, although in a dissenting judgment, that should a director make a bad business decision based on his inexperience, he cannot be held accountable.[120] It is submitted that this view is the correct one in so far as the director cannot reasonably become acquainted with the subject matter and as a result eliminate or at the very least alleviate that inexperience. It should also be noted that mere inexperience is not a sufficient defence in all situations. Should directors make a bad business decision in a situation where they should not be making such decisions, *in casu*, where the company is insolvent and the directors were explicitly told not to engage in business activities, inexperience may not be a valid excuse and the directors may be held liable.[121]

Diligence again appears to be an objective test as one should objectively determine whether the director has given his duties due attention. It is important to show the correlation between the objective and subjective elements. Cassim states that the subjective standard will only be taken into account where it improves upon the objective standard and thereby raises the bar of what can be expected of that director.[122] According to De Jager, the Banks Act has a similar provision: that the objective standard is the minimum standard and that the subjective standard serves only to raise the standard above the objective standard and never below it.[123]

Case law generally appears to take the holistic approach with concepts of care, skill and diligence and discusses them as such. In *Fisheries Development Corporation of South Africa Ltd v Jorgensen and another* it was held that these duties imply that a director may not be indifferent or a mere puppet and that he may not shelter behind an inability to understand the company's affairs.[124] It has also been held that a director has a duty to observe the utmost good faith towards the company and

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117 S76(3)(c)(ii).
118 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 559.
119 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 559.
120 Multinational Gas & Petrochemical Co Ltd v Multinational Gas & Petrochemical Services Ltd [1983] Ch 258 at [504].
121 See generally West Mercia Safetywear Ltd v Dodd [1988] BLCL 250 (CA).
122 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 559.
123 De Jager, 2005 SA MERC LJ 170 (citation needed).
124 Fisheries Development Corporation of South Africa Ltd v Jorgensen and Another; Fisheries Development Corporation of South Africa v AWJ Investments (Pty) Ltd and Others 1980 (4) SA 156 at p158.

that from this the duty to exercise reasonable care and skill arises.[125]

The Business Judgment Rule

Section 76(4) contains the so-called Business Judgement Rule (BJR hereafter). The BJR was developed as a counterweight to the duties of care and skill. According to Bouwman, the BJR serves many purposes but four of the most important are as follows:

1. A company's growth may be stifled if a director is unwilling to engage in any activity which has an element of risk. The BJR allows a director to take reasonable risks without fear of incurring personal liability, the net result of which encourages growth within a company.
2. The protection offered by the BJR may be sufficient to entice competent persons into the position of director.
3. It is to avoid “judicial second guessing”. When brought before a court, a judge assesses a director's actions. Bouwman states that this is unfair towards the director since “judges are experts in law not in business practice” and “judges have the benefit of hindsight”. Without the BJR, this may entail that a director be judged quite harshly despite having acted to the best of his abilities.
4. Finally, it is also there to prevent the shareholders from managing the company. Without the BJR, shareholders may be encouraged to litigate more frequently and thereby manage the company. However, with the rule in place, the risk and the costs involved serve as strong discouraging elements against frivolous litigation.[126]

The result of a director complying with all of the requirements is that the merits and wisdom of his decision falls outside judicial review.[127] It protects a director who made a decision based on the information at his disposal, but facts revealed later rendered that decision unreasonable or imprudent.[128] Most importantly, it protects such a director from personal liability and it provides no protection to dishonest or fraudulent directors.[129]

For ease of reference, section 76(4) which encompasses the BJR in the new Act is as follows:

(4) In respect of any particular matter arising in the exercise of the powers or the performance of the

125 Howard v Herrigel and Another NNO 1991 (2) SA 660 (A) at p674.
126 An Appraisal of the Modification of the Director's Duty of Care and Skill, N Bouwman, SA Mercantile Law Journal, 2009, p523-524.
127 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 565.
128 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 565.
129 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 565-566.

functions of director, a particular director of a company—

(*a*) will have satisfied the obligations of subsection (3) (*b*) and (*c*) if—

(i) the director has taken reasonably diligent steps to become informed about the matter;

(ii) either—

(*aa*) the director had no material personal financial interest in the subject matter of the decision, and had no reasonable basis to know that any related person had a personal financial interest in the matter; or

(*bb*) the director complied with the requirements of section 75 with respect to any interest contemplated in subparagraph (*aa*); and

(iii) the director made a decision, or supported the decision of a committee or the board,with regard to that matter, and the director had a rational basis for believing, and did believe, that the decision was in the best interests of the company;

Firstly, the section limits itself only to where the director exercises the power, performance and functions of a director. From the wording of this section 76(4)(a), it appears as if the BJR as stated in the Companies Act serves both as a definition and as an overriding test. The overriding nature will be discussed below. As a definition, it gives content to some of the abstract phrases contained in section 76(3)(b) and (c). At the same time, it appears that even where a director failed the tests contained in sections 76(3)(b) and (c), the overriding nature of section 76(4)(a) would allow a director to escape liability should he comply with the BJR.

In order for section 76(4)(a) to come into operation, the director must fulfill its requirements. Firstly, it requires a director to have taken reasonably diligent steps to become informed on the matter.[130] Levenstein states that this duty would be complied with if the director relies upon information brought before him by an employee to whom the responsibility to perform the board's functions has been delegated.[131] He further states that the director is entitled to rely upon the information as well as the truthfulness thereof.[132] However, as is shown below, this is not entirely true since a director cannot simply adhere to such information based solely on the fact that it was brought before him by an employee.

The second requirement relates to financial interests. A director should not have any financial interests in the outcome of the decision, nor should he be aware that a party related to him has a

130 S76(4)(a)(i).
131 The Personal Liability of Directors, E Levenstein, Without Prejudice Issue 5, 2011, p21.
132 The Personal Liability of Directors, E Levenstein, Without Prejudice Issue 5, 2011, p21.

financial interest in the outcome.[133] A director is deemed to be related to another person who he is married to or separated from by no more than two degrees of natural or adopted consanguinity or affinity from a natural person.[134] Where the related person is a juristic person, it refers to where a director either directly or indirectly controls that juristic person.[135] Should a director or party related to the director have a financial interest to the outcome, the BJR may still apply if the director had complied with the provisions regarding disclosure of financial interests as set out in section 75.[136]

The third requirement is a hybrid test.[137] The objective element looks at the basis for the decision made by the director. It requires that, at a logical assessment by a reasonable director, that reasonable director would also decide that the decision is in the best interests of the company. The subjective element requires that the director himself must have believed that his decision, based upon the information before him, was in the best interest of the company. Delport states that fault has now become an element for breach of fiduciary duties.[138] It is also interesting to note that proper purpose plays no part in the BJR.[139]

Without going into too much detail, the remainder of S76 allows a director to rely upon the information placed before him and the performance of committees, employees, legal council, accountants and other professional persons, as well as their opinions, recommendations, information, reports and statements.[140] However, a director may not follow this information blindly. The director must reasonably believe that the person referred to above is both competent and reliable.[141] This again, is an objective test.

Overriding Nature of the Business Judgment Rule

Bouwman argues that the BJR should not have been included.[142] She further states that the lines between the test for breach of care and skill (CAS hereafter) and the BJR have become blurred,

133 S76(4)(a)(ii)(aa).
134 S2(a).
135 S2(b).
136 S76(4)(a)(ii)(bb).
137 S76(4)(a)(iii).
138 The New Companies Act Manual Including Close Corporations and Partnerships (Student Edition), P. Delport, Lexis Nexis, 2011, p94.
139 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 564.
140 See generally S76(4)(b) and S76(5).
141 S76(5)(a).
142 An Appraisal of the Modification of the Director's Duty of Care and Skill, N Bouwman, SA Mercantile Law Journal, 2009, p534.

since both refer to the duty to act in the best interest of the company.[143] It is submitted, contrary to what Bouwman states, the mere fact that both tests share a common element does not automatically mean that the BJR's intention was to replace or dilute the CAS duties.[144]

Firstly, despite sharing a common element, the BJR and CAS each test for different things. Briefly paraphrased, the CAS tests for good faith, proper purpose, best intentions and the care and skill requirements. Likewise, the BJR tests for whether the director became properly informed, made the necessary financial disclosures and whether there was a rational basis for believing that the decision was in the best interest of the company. Furthermore, the tests under CAS are much more stringent, while BJR's are much more lenient. Also, the BJR does not exclude the good faith and proper purpose requirements contained in section 76(3)(a).[145]

Secondly, the underlying requirements are different for the test for best interest. It is submitted that the requirement contained in section 76(3) for acting in the best interest of the company is an objective test, while the BJR's test for this is subjective. The BJR's subjective nature is clear from its wording of the phrase "the director had a rational basis for believing".[146] In other words, that specific director must have subjectively believed that the decision was objectively in the best interest of the company. Viewed in this light, the test is precisely defined as whether, in the mind of that director, he had complied with the requirements of best interest in the company contained in S76(3)(b). Again, this shows that the BJR does not intend to replace the care and skill tests, since without the CAS test the BJR would lose context. This is so because it refers to an element of CAS, which also naturally implies the rich history associated with it is also applicable.

Thirdly, section 76(3) forms the departure point for determining a director's liability. The BJR only comes into effect once a director has failed in his CAS duties. This can be deduced from the wording of the BJR. It states that section 76(3)(b) and (c) will be deemed to have been complied with should the director fulfill the requirements of the BJR.[147] The focus is still clearly on section 76(3) and as such, the intention of the BJR is to form a secondary limitation on the liability of directors instead of creating a replacement for the requirements of CAS. Therefore, the BJR should

143 An Appraisal of the Modification of the Director's Duty of Care and Skill, N Bouwman, SA Mercantile Law Journal, 2009, p529.
144 An Appraisal of the Modification of the Director's Duty of Care and Skill, N Bouwman, SA Mercantile Law Journal, 2009, p529.
145 S76(4)(a).
146 S76(4)(a)(iii).
147 S76(4)(a).

only come into effect once the CAS tests have been failed by a director. The net effect is that the BJR does not override CAS as much as it serves to augment it. It attempts to keep the protective measures in CAS active but also recognizes the practical challenges faced by directors in the day-to-day operation of a business. Read together, it is submitted the BJR and the duties of CAS provide realistic and sufficient limitations on the powers of directors' actions.

CHAPTER 4

COMMON LAW LIMITATIONS ON A DIRECTOR'S DUTIES

Introduction

Since director's duties are only partially codified and the common law is not specifically excluded, the rules contained in the common law remain relevant and of utmost importance. Moreover, it is submitted that the common law is the best vehicle for the future development of company law. The courts have a duty placed upon them to develop the common law to enable individuals enjoy the rights and ideals established by the Act.[148] As a result, courts may quickly and efficiently adapt the common law to close any shortfalls in the Act without going through the lengthy amendment process. This grants great flexibility should the need arise. However, it is submitted that the courts should take care with this power and exercise it conservatively lest the well-established company common law become diluted or lose efficacy because of a new interpretation.

Each of the discussed sections has a common law equivalent. While the legislative versions have kept these duties more or less the same, there are other duties found solely in common law. For a director to know how to act and to avoid all liability, he would do well to be aware of these duties as well.

For fiduciary duties, the basis of liability common law level originates in the fiduciary relationship between the company and the director.[149] As such Delport states that the source of liability is neither delictual or contractual but comes from a breach of trust.[150]

There is already a large body of work available on this topic. For the sake of brevity, the content of the common law will only be briefly touched upon.

Conflict of Interest

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148 S158.

149 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p131 at 13.85.

150 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p131 at 13.85.

A conflict of interest arises where an individual's pursuing either their own interests or the interests of another party would result in harm, damage or loss to the interest not followed. Delport states that there is a legal duty placed upon directors to prevent such a conflict of interest.151 This corresponds with section 76(2)(a), which essentially deals with the issue of conflict of interest. In terms of common law, a director is allowed no other advantage from his office other than his agreed-upon remuneration.[152] This rule applies equally to any secret profits made, even where they are obtained in good faith and cause no harm to the company.[153] The primary consideration is whether these advantages' source originated from the office of director.[154] Similar to section 76(2)(a), a director may not use any information gained to his personal advantage or profit.[155]

Cassim subdivides the care and skill rule into two distinct but closely related elements or duties:

- The duty to avoid a conflict of interest (the no-conflict rule) and
- The duty not to make a profit (the no-profit rule).[156]

The no-profit rule entails that a director may not retain any profit made by the virtue of his office, that he must disgorge all profits made in this manner and that the term profit is not limited to money.[157]

Cassim also includes the corporate opportunity rule into the duties contained in the care and skill rule.[158] This rule prohibits a director from or usurping any contract, information or other opportunity that properly belongs to the company and came to him as director or pursuing any opportunity which is said to fall within a company's existing or prospective business opportunities.[159]

The defences available to a director are very limited and strict. The only way for a director to avoid

151 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p131 at 13.87.
152 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p131 at 13.87.
153 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p131 at 13.88.
154 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p131 at 13.88.
155 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p132 at 13.99.
156 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p535.
157 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p536.
158 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p538.
159 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p538.

liability is for his principal (the company) to give its free consent after full disclosure.160 It is submitted that this defence will still be available to directors even where they are held liable in terms of a breach of S76(2)(a).

While it may seem counter intuitive, a person may simultaneously be a director of two competing companies as long as he does not use confidential information obtained from one company to benefit another.[161] This is however subject to certain limits. From the *Atlas Organic Fertilizers* case, it is submitted that the general rule regulating this type of situation is based on considerations of common sense.[162] It was held that common sense dictates that a director cannot be the managing director of two companies simultaneously.[163] It is submitted that the reasons for this ruling is that, from a logistical standpoint, it is impossible for a director to give the due regard to each company as required by his fiduciary duties and the challenge faced by a director not to use information gained *ex officio* from one company to the benefit of another. However, it was also held that it is permissible for a director to become the director of a competing company where he has served his notice of termination of employment and is simply still working at the first company for the notice period.[164] A director is entitled to seek other employment opportunities even where his contract is in the process of being terminated and even at a competing company.[165] It is submitted that simultaneous employment at competing companies can be possible in situations other than the one stated above. The key consideration remains whether or not common sense permits that the director will be able to fulfill all of his obligations and fiduciary duties to both companies at the same time. However, where a director is a director for two competing companies, the mere knowledge of the prices or the making of an offer by a director of one company may automatically mean that he is acting to the detriment of the other company.[166]

Exceeding the Limits of Granted Powers

At common law, a director must exercise his powers within certain prescribed limits. Should a director act outside the limitations placed on his own authority, he may be held personally liable for

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160 Phillips v Fieldstone Africa (Pty) Ltd (2004) All SA 150 SCA at para 31.
161 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p133 at 13.91.
162 Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd 1981 (2) SA 173 (T) at [198].
163 Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd 1981 (2) SA 173 (T) at [199].
164 Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd 1981 (2) SA 173 (T) at [199].
165 Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd 1981 (2) SA 173 (T) at [199].
166 Sibex Construction (SA) (Pty) Ltd v Injectaseal CC 1988 (2) SA 54 (T) at [67].

any loss suffered.[167] Cassim states, although not explicitly, this rule still forms part of section 76, since this duty forms part of the good faith and proper purpose duties of a director.[168]

However, it is possible for a director to bind a company even where he is not authorized to do so due to the operation of the Turquand rule.[169] The Turquand rule originated in the British case of *Royal British Bank v Turquand*.[170] The rule states, "each outsider contracting with the company in good faith is entitled to assume that all internal requirements and procedures have been complied with".[171]

Under common law, the Turquand rule operated alongside the doctrine of constructive notice. This doctrine held that everyone dealing with a company is presumed to be fully acquainted with the public documents of that company.[172] But, despite being acquainted or deemed acquainted with the public documents, it is not always possible for a third party who is dealing with a company to know whether the internal requirements of a company have been met.[173] An example of such an internal requirement would be where the articles of association state that a board meeting must have been held and that the board must have approved an agreement before the company may proceed whilst the third party had no way knowing what the outcome of that meeting was.[174]

The Turquand rule now allows that third party to assume all internal requirements were met and that the actions of the company were valid and not performed *ultra vires*. However, the Turquand rule is not an absolute rule. It does not apply in circumstances where the outsider knew that there was an irregularity andthat there were internal requirements (therefore acting in bad faith) or where the circumstances were suspicious.[175]

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167 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p133 at 13.92.

168 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 533.

169 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p133 at 13. 93.

170 (1856) 6 E&B 327.

171 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p151 at 14.28.

172 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p147 at 14.10.

173 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p150 at 14.27.

174 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p150 at 14.27.

175 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p151 at 14.29.

The Act has partially abolished the doctrine of constructive knowledge. In section 19(5), it states that the public is only deemed to know the contents of the constitutive documents or memorandum of incorporation of a company if it has the abbreviation “RF” in its name.[176] In such a case, the new statutory Turquand comes into effect. It is essentially the same as the common law Turquand, save for the fact that it states specifically that this rule cannot apply to directors, prescribed officers or shareholders.[177]

This is of importance to directors since it again shows that directors are only permitted to operate within the sphere of the authority given to them. Should they exceed it, their defences are limited and the fact that they had no authority will not protect them from being held personally liable in terms of section 77.

Failure to Maintain an Unfettered Discretion

A director must act objectively towards the company and should not be forced to act in a certain manner by a third party.[178] Cassims states that the director must act in an unbiased and objective manner.[179] Some commentators see this duty as part of a director's duty to act in good faith.[180] Cassim theorises that this is why it was not explicitly included in sections 76(2) and (3), since the duty to exercise independent judgment is implied to form part of a director's fiduciary and statutory duties.[181] As such, a contract between a third party and a director which stipulates that a director must vote in a specific way is unenforceable against the director.[182] However, this rule is not absolute. The overriding principle is that the director should act in the best interest of the company.[183] Therefore, should it be in the best interests of the company that a director be bound by such a contract requiring him or her to vote in a specific manner, then it would be permissible.[184]

176 S19(5).
177 S20(7).
178 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p133 at 13.95.
179 Contemporary Company Law 2nd Edition, FHI Cassim et al, Juta, 2012, p529.
180 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 529.
181 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 529.
182 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p133 at 13.95.
183 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p134 at 13.96 read with Fisheries Development Corporation of SA Ltd v Jorgensen 1980 (4) SA 156 (W) at 164F.
184 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p134 at 13.96 read with Fisheries Development Corporation of SA Ltd v Jorgensen 1980 (4) SA 156 (W) at 164F.

There are, however, important consequences for nominee directors. A nominee director is appointed to represent another director in some or other capacity, whether only for a single meeting or on a more permanent basis.[185] Since the nominated director is deemed to be a *de jure* director, he may find himself in the untenable position of having the interests of his principal and the interests of the company conflicting with one another seeing as he has a duty towards both.[186] However, it was held that in such a situation, the nominee must serve the interests of the company to the exclusion of any nominator, employer or principal.[187]

Failure to Exercise Powers for which They were Given

This rule deals with the proper purpose phrase found in section 76(3)(a) and is essentially the same. It states that a director must exercise their powers for the purpose that they were given.[188] The simplest example again is the issue of shares. Directors may only issue shares for generating capital and not for affecting or manipulating control of a company or defeating a pre-existing majority.[189]

Duty of Care and Skill

The common law CAS duties are similar to the ones contained in the Act. The main difference is that the Act also requires the element of diligence while common law does not. As in the Act, 'care' refers to an objective test while 'skill' refers to a subjective one.[190] The meanings of 'care' and 'skill' are the same as was explained in Chapter 3 *supra*, namely that skill refers to aptitude while care refers to how that aptitude is applied.

The fundamental principles of CAS were stated in the *Fisheries Development of SA Ltd v Jorgensen* case.[191] It summarised the CAS duties into three broad principles:

1. The extent of the CAS duties placed upon a director depends largely upon the nature of the business that the company engages in as well as the nature of the duties assigned to that director. A higher burden is placed upon an executive director than on a non-executive

185 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 529.
186 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p 529.
187 Fisheries Development Corporation of SA Ltd v Jorgensen; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd 1980 (4) SA 156 (W) at 163.
188 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p134 at 13.98.
189 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p134 at 13.98 and 13.99.
190 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p135 at 13.100.
191 1980 (4) SA 156 (W).

director, since the non-executive director's duties are intermittent in nature.

2. No special business acumen, singular ability or skill is required before becoming a director. A director can only be expected to act in a manner which can be reasonably expected from that particular director.
3. A director may rely upon information given to him from an employee unless there are specific grounds for suspicion. However, this does not entitle a director to blindly trust such information.[192]

However, it may be noted that the mere fact that a director is classified as either an executive or non-executive director is not sufficient to alter the duties of care and skill.[193] The main determining factor remains the facts and circumstances surrounding the day-to-day activity of a director.[194] The Act has to a large extent echoed this judgment in sections 76(4) and 76(5).

The basis for a claim against a director who has failed his CAS duties is based upon Aquilian liability for negligence.[195] Therefore, should a director breach his duty of CAS, he may be held liable in terms of delict.[196] If there was a contract between the director and the company, it may very well be that the director had committed a breach of contract as well and he may also be sued under a contractual action.[197]

192 1980 (4) SA 156 (W) at 165 to 166 read with Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p135 at 13.101.
193 Howard v Herrigel and Another NNO 1991 (2) SA 660 (A) at p678.
194 Howard v Herrigel and Another NNO 1991 (2) SA 660 (A) at p678.
195 Contemporary Conpany Law 2nd Edition, FHI Cassim et al, Juta, 2012, p555.
196 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p135 at 13.102.
197 Entrepreneurial Law Incorporating the New Companies Act (Special Edition), ML Benade et al, Lexis Nexis, 2009, p135 at 13.102.

CHAPTER 5

CONCLUSION

Section 66 is the main point of departure and it is the cornerstone of the powers and authority of directors. It empowers directors to act and move the company as they deem best. Despite not being given a concrete definition in legislation or by the courts, it is clear that the term “manage the business and affairs” in section 66 grants the directors wide and sweeping powers over almost every aspect of a company. The section further empowers the director to perform any actions and functions of the company. This also allows a director to bind the company in legal transactions. However, such powers cannot go unregulated. Within section 66 itself, the foundations for such regulations have already been laid out. Despite them having wide powers by default, they are still reined in by the Act itself (specifically section 76) and can be tampered by the company's memorandum of incorporation.

The limitation on the powers of directors stem from the fiduciary relationship between the directors in their professional capacity and the company. These restrictions are contained in common law and legislature, and the director must comply with both. The definition of ‘director’ does not solely refer to the individuals designated as such, and it is therefore much wider in its scope. It may include alternate directors, prescribed officers, certain employees and even individuals who are not directors by designation but are act like directors in all but name. This is important since all individuals who are deemed to fall within the definition of director must either comply with the restrictions, duties and limitations placed on directors or they must face the negative consequences of non-compliance.

The first major restriction comes in the form of the limitation on the use of information as stated in section 76(2). A director may not use information gained by virtue of his office for personal gain. The common law equivalent prohibition on the conflict of interest operates generally on the same principles. Of key importance, it is submitted that a director may avail himself to the common law defence of full disclosure to protect himself from a statutory breach and consequent personal liability. While this is a logical and good limitation, section 76(2)(a)(ii) also places a new duty on directors, namely that they may not act to the detriment of a subsidiary in certain instances. This is an anomaly since classically directors only owe a duty towards the company which employed them. As stated in Chapter 3, this is excessively wide but appears to be circumventable in certain instances. Section 76(2) also places a duty on the director to convey certain kinds of important information to the board. It should also be noted this communication is not absolute and a director need not communicate every single piece of information that comes to his attention. For example, information which is already public knowledge or known by the other directors need not be repeated.

A director must also use his powers in good faith and for proper purpose in terms of section 76(3). Good faith is a subjective test. Proper purpose refers to using the powers only for the reasons they were granted. The proper purpose requirement is also reflected in common law. In addition, a director must use their powers in the best interest of the company as stated in section 76(3)(b). However, this is not an absolute rule as the best interest of a company may be held in abeyance in favor of third party stakeholders which may in the long term yield a greater profit for the company. Finally, there is the duty of care, skill and diligence as contained in section 76(3)(c). It is a hybrid test which measures the actions of a director both subjectively and objectively. It ensures that a director acts within the range of what can reasonably be expected of a person in that position of power. Again, to a large extent it reflects the care and skill tests found in the common law, save for the fact that the statutory version has added the requirement of diligence.

In section 76(4) the BJR has been incorporated into South African law. It encourages directors to take reasonable risks to ensure growth in the company without fearing personal liability should the venture fail. It also protects the director from judicial second-guessing. It is respectfully submitted that the BJR does not override the duties of care and skill, but rather augments them, allowing for practical and realistic governance of directors.

Section 76(5) provides another safe harbour for directors where they relied upon the information put before them by an employee or committee in so far as the information appears reasonable and reliable.

At common law there is also the duty not to exceed the limitation of the authority granted to directors. In addition, there is the rule that a director should not fetter their discretion. However, it may be permissible to do so where such fettering would be in the best interest of the company.

Ultimately, all of the rules and limitations based upon directors come back to the basic principle that a director must always act honestly and in good faith. It is submitted that even directors with little knowledge of company law can navigate the vast majority of difficult decisions by keeping that simple principle in mind. Yet, despite all of the limitations placed upon directors, they still retain ultimate power over a company. These limitations are by and large fair yet necessary. It is submitted that both the scope and limitations of powers and authority conferred on directors by the new Act are generally well thought out, practically applicable and take the real challenges faced by directors into account. The inclusion of the common law adds much flesh to the legislature, allowing a long-standing and rich history of legal jurisprudence to remain in force. It is submitted that the Act may not be a perfect piece of legislation, however, it seems to be aware of that fact since it allows shortfalls to be mended quickly by courts. It is further submitted that the Act might not have succeeded in all of its goals set out in section 7 but it definitely is a step in the right direction.

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