

*'DELINQUENT DIRECTORS' AND 'DIRECTORS UNDER PROBATION': A UNIQUE  
SOUTH AFRICAN APPROACH REGARDING DISQUALIFICATION OF COMPANY  
DIRECTORS*

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**Abstract**

*This article explores the unique way in which disqualification of company directors are provided for in the South African Companies Act 71 of 2008. Not only are the terminology like 'delinquent director' or 'director under probation' unique, but there are also several peculiar aspects regarding the orders that a court can make, and conditions attached to these orders, when persons are declared 'delinquent' or put under 'probation' by a Court. The article also explains in detail the rather complex nature of the disqualification provisions and it analyses all the decided cases dealing with 'delinquency'. The focus is in particular on the constitutionality of the 'delinquency' orders by a Court, a pivotal aspect in most of the cases decided so far. It is concluded that the core problem of the section providing for the disqualification of persons on application (section 162 of the 2008 Act) is its complexity. Different parties have standing to apply for delinquency or probation orders respectively, and the circumstances under which these parties can apply for such orders are also different and require careful interpretation to comprehend. It is pointed out that it is unlikely that these provisions will be used to their full potential to achieve the ultimate goals with them, namely the protection of shareholders, creditors and the public against delinquent directors and to provide opportunities for some directors to gain experience as directors under Court orders placing them 'under probation'.*

**1. Introduction**

Company law legislation in all modern company law systems have provisions dealing with the disqualification of company directors. Traditionally a distinction is made between automatic

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disqualification grounds (currently contained in section 69 of the South African Companies Act 71 of 2008 ('the 2008 Act')) and grounds on which persons could be disqualified by a Court order even though the person is not automatically disqualified. Section 219 of the former South African Companies Act 61 of 1973 ('the 1973 Act') was the section dealing with disqualification by Court order. The reason why the 2008 Act is not used to illustrate the difference between the two types of disqualification, is that the 2008 Act adopted an almost completely new approach regarding disqualification of directors by a Court order, on application by several parties.<sup>1</sup> The current section that could generally be described as the disqualification by Court order provision, is section 162 of the 2008 Act.<sup>2</sup> This section is, however, a distinctive South African provision with no exact counterpart in any other jurisdiction. The heading of the section is 'Application to declare director delinquent or under probation', suggesting some peculiarities if one appreciates that a 'delinquent' director is disqualified from acting as a director for the period the Court determined.

In this article we will examine this section in order to determine what the aims of the legislature were with it. The section is unique for several reasons, not least for using the terminologies like 'delinquent director' and 'director under probation'. In addition, there is to our knowledge no other jurisdiction where so many different parties have standing to apply for orders to declare a director a 'delinquent' or placing a director 'under probation'. We will also draw the attention to the provision regarding 'conditions' that may be stipulated by a Court that may be 'applicable or ancillary'<sup>3</sup> to orders declaring persons 'delinquent' or 'under probation'. The focus will also be on the periods a person could be declared 'delinquent' or the period a person can be placed 'under probation'. Other unique aspects that will be touched upon are the circumstances under which delinquent or probation orders could be suspended or the possibility of a delinquent order being substituted by an order of probation. An analysis of the cases decided under section 162 will be undertaken in Parts 7 and 8. We will conclude by speculating whether the aims with the section are achievable and realistic as part of modern company law legislation.

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<sup>1</sup> See Part 2 below.

<sup>2</sup> S 162 of the 2008 has not been the subject of any in-depth analysis in South Africa, although several sources would provide a basic summary and overview of the section. See, for example Rehana Cassim 'Governance and the board of directors' in Farouk HI I Cassim (managing ed) *Contemporary Company Law* 2n ed (2012) 435-439.

<sup>3</sup> S 169(10) of the 2008 Act.

## 2. Overview and standing to apply for orders or declarations

Section 162 of the 2008 Act is a very long section with approximately 1,500 words. It commences by defining the term ‘legislation’ very widely, including any national and provincial legislation:

- (a) relating to the promotion, formation or management of a juristic person;
- (b) regulating an industry or sector of an industry; or
- (c) imposing obligations on, prohibiting any conduct by, or otherwise regulating the activities of, a juristic person.

A ‘juristic person’ as defined in section 1 of the 2008 Act includes a foreign company, and a trust, irrespective of whether or not it was established within or outside the Republic. A ‘foreign company’ is defined, also in section 1, as an entity incorporated outside the Republic, irrespective of whether it is a profit, or non-profit, entity or whether it is carrying on business or non-profit activities, as the case may be, within the Republic. Section 162 can therefore, theoretically at least, be applicable to a foreign company, but if it is not subject to certain provisions of the 2008 Act because it is registered as an external company in terms of section 23(2) of the 2008 Act, it is not clear how section 162 can be applicable.<sup>4</sup> Even if it is so registered, the legal personality and appointment and removal of directors will be regulated by the laws of its country of incorporation and would therefore not be subject to section 162.<sup>5</sup> Although a South African trust is not ‘promoted’ or ‘formed’ in terms of national legislation, its management is regulated by such legislation.<sup>6</sup> However, whether trustees will be ‘directors’ as defined in terms of the 2008 Act is doubted. What is apparently intended to be included are certain entities that are juristic persons in terms of a particular Act, such as the South African Broadcasting Corporation Limited which is deemed to be a company incorporated in terms of the (1973) Companies Act<sup>7</sup> and which will have directors, by inference, as defined in section 1 of the Companies Act.<sup>8</sup> Although there are other entities that must be registered as companies

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<sup>4</sup> In respect of a foreign company the only applicant can, in terms of s 162(4), be an organ of state.

<sup>5</sup> See for the foreign and external company also Piet Delport, *Henochsberg on the Companies Act 71 of 2008*, Loose Leave Service (2016) 107.

<sup>6</sup> Trust Property Control Act 57 of 1988. Although a trust does not have separate legal personality in terms of common law, it is included in the definition of a ‘juristic person’ in s 1 of the 2008 Act.

<sup>7</sup> S 8A(1) of the Broadcasting Act 4 of 1999.

<sup>8</sup> See *Mpofu v South African Broadcasting Corp Limited (SABC) and Others* (2008/18386) [2008] ZAGPHC 413 (16 September 2008) para 29; *South African Broadcasting Corporation Ltd v Mpofu and Another* [2009] 4 All SA 169 (GSJ) para 20.

to effect business,<sup>9</sup> the critical issue is whether the person responsible for the administration will be an organ of state<sup>10</sup> as required by section 162(4) of the 2008 Act.

The section then lists the parties who have standing to bring an application under this section and then deals with the requirements and consequences of orders to declare a director 'delinquent' or 'under probation'. It also contains the grounds on which persons could be declared as such and that the court can add conditions to these orders.

The following persons may approach a court for a person to be declared 'a delinquent' or 'under probation':<sup>11</sup> The company; a shareholder; a director; a company secretary; a prescribed officer of the company; a registered trade union of the company; an employee representative scheme; the Companies and Intellectual Property Commission (hereafter 'Commission')<sup>12</sup> and the Takeover Regulation Panel (hereafter 'Panel'); and any organ of the state<sup>13</sup>. These applicants can bring an application to a court for an order declaring a person delinquent or under probation if he or she is a director of a company or, within 24 months immediately preceding the application, was a director of a company.<sup>14</sup> The parties who are mentioned first to have standing to bring an application under section 162 are the company, as separate legal entity, and several other internal persons or parties, namely a shareholder, a director a company secretary and a prescribed officer. The fact that 'a registered trade union that represents employees of the company or another representative of the employees of a company' has standing to bring an application under section 162 is without parallel in any other jurisdiction. The potential of putting directors under considerable pressure by trade unions or employees and their representatives must be apparent. Even the application of an order to declare a director as a 'declared delinquent' (see discussion below) will be distressing for most directors even if they

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<sup>9</sup> See for example the Long Term Insurance Act 52 of 1988 and the Short Term Insurance Act 53 of 1988, administered, *inter alia*, in terms of the Financial Services Board Act 97 of 1990.

<sup>10</sup> S 1 of the 2008 Act incorporates s 239 of the Constitution of the Republic of South Africa 108 of 1996 ('Constitution') regarding 'organ of state'. In 239 'organ of state' is defined as follows:

- a. any department of state or administration in the national, provincial or local sphere of government;
  - or
  - b. any other functionary or institution
    - i. exercising a power or performing a function in terms of the Constitution or a provincial constitution; or
    - ii. exercising a public power or performing a public function in terms of any legislation,
- but does not include a court or a judicial officer;

See further *Minister of Education, Western Cape v Governing Body, Mikro Primary School* 2006(1) SA 1 (SCA); *Mittalsteel South Africa Ltd (formerly Iscor Ltd) v Hlatshwayo* 2007 (1) SA 66 (SCA); *Katshwa v Cape Town Community Housing* 2014 (2) SA 126 (WCC) para 14.

<sup>11</sup> S 162(2) of the 2008 Act.

<sup>12</sup> Established under s 185 of the 2008 Act.

<sup>13</sup> As far as 'organ of state' is concerned, see footnote 10 above.

<sup>14</sup> Ss 162(2)(a), 162(3)(a) and 162(4)(a) of the 2008 Act.

know that there is little chance of a court in fact ordering them to be delinquent on the application of these parties.

Under sections 162(3) and (4) of the 2008 Act the Commission, the Panel and ‘[a]ny organ of state responsible for the administration of any legislation’ also have standing to bring an application under section 162. Perhaps nothing should be made of the order in which parties with standing to bring these applications are mentioned, but the impression could be created that under the 2008 Act the responsibility of bringing these applications rests primarily on the shoulders of the ‘other parties’, not on the Commission, the Panel or any other organ of state responsible for the administration of any legislation.

### **3. Orders under section 162 of the 2008 Act**

#### **3.1 Order to declare a person a ‘delinquent’**

It should be noted that a unique distinction is made between an order to declare a person ‘delinquent’ (discussed here) and an order to place a person under ‘probation’ (discussed in Part 3.2 below). As far as applications to declare a person a delinquent is concerned, a court *must*<sup>15</sup> make an order declaring a person to be a delinquent director if the person was disqualified while acting as a director or member of a close corporation (under section 69 of the 2008 Act and section 47 of the Close Corporations Act 69 of 1984 (‘Close Corporations Act 1984’))<sup>16</sup> and such an order *must* also be made by the court if the person, while being a director:<sup>17</sup>

- consented to serve as a director, or acted in the capacity of a director or prescribed officer, while ineligible or disqualified in terms of section 69;<sup>18</sup>
- contravened an order of probation in terms of either section 162(7) of the 2008 Act or section 47 of the Close Corporations Act 1984;
- grossly abused the position of director, took personal advantage of information or an opportunity (contrary to section 76(2)(a) of the 2008 Act);

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<sup>15</sup> See discussion under Part 8 in respect of the lack of discretion of the court.

<sup>16</sup> S 262(5)(a) and (b) of the 2008 Act.

<sup>17</sup> See s 162(5) of the 2008 Act.

<sup>18</sup> S 162(5)(a) of the 2008 Act – there are exception pertaining to persons acting under the protection of a court order contemplated in section 69(11) of the 2008 Act as a director as contemplated in section 69(12) of the 2008 Act.

- intentionally, or by gross negligence, inflicted harm upon the company or a subsidiary of the company (contrary to section 76(2)(a)); or
- acted in a manner that that amounted to gross negligence, willful misconduct or breach of trust in relation to the performance of the director's functions within, and duties to, the company; or in a manner specifically provided for and where the director would be liable for any loss, damages or costs sustained by the directors because of specified wrongful acts (listed in section 77(3)(a)-(c) of the 2008 Act.

Another peculiarity and complexity of section 162 is that, although there is some overlap, there are different grounds stipulated under which 'the Commission and Panel', 'any other organ of state responsible for the administration of any legislation' and 'other parties' respectively may apply for a person to be declared a delinquent.<sup>19</sup> For instance, it is only 'the Commission and Panel', 'any other organ of state responsible for the administration of any legislation' that can apply for a delinquency order based on the fact that the person against which the order is sought has repeatedly been personally subject to a compliance notice or similar enforcement mechanism, for substantially similar conduct, in terms of any legislation.<sup>20</sup> The 'other parties' have no standing to apply for a delinquency order on this ground, probably also because they will have no knowledge of non-compliance and will not be able to prove it without access to the records of the Commission or Panel.

### **3.2 Order to place a person under 'probation'**

Some additional requirements are stipulated, linked to specific situations, before a court can place a director or the managing member of a close corporation under probation.<sup>21</sup> For instance, the court must be satisfied that the declaration is justified, having regard to the circumstances of the company's or close corporation's failure, and the person's conduct in relation to the management, business or property of the company or close corporation at the time.<sup>22</sup> Also, it should be noted that a probation order could contain any conditions appropriate, including conditions limiting the application of the declaration to one or more particular categories of companies.<sup>23</sup>

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<sup>19</sup> See and compare s 162(2)(b), s 162(3)(b) and s 164(4) of the 2008 Act.

<sup>20</sup> See and compare again s 162(2)(b), s 162(3)(b) and s 164(4) of the 2008 Act.

<sup>21</sup> S 162(8) of the 2008 Act.

<sup>22</sup> S 162(8)(b)(ii) of the 2008 Act.

<sup>23</sup> S 162(9)(a) of the 2008 Act. A director of multiple companies could therefore be under probation only in respect of a single company.

On application of any of the ‘other parties’, the Commission, or Panel (‘an organ of state responsible for the administration of any legislation’ has no standing under this section) a court has a *discretionary* power under section 162(7)(a) of the 2008 Act to make an order placing a person under probation, if, while serving as a director, the person:

- (i) was present at a meeting and failed to vote against a resolution despite the inability of the company to satisfy the solvency and liquidity test, contrary to this the 2008 Act;<sup>24</sup>
- (ii) otherwise acted in a manner materially inconsistent with the duties of a director;<sup>25</sup> or
- (iii) acted in, or supported a decision of the company to act in, a manner contemplated in section 163(1) of the 2008 Act.

On application of the Commission or Panel (the other parties mentioned above do not have standing under this section), section 162(7)(b) of the 2008 Act gives a court the discretionary power to place a person *under probation* if within any 10-year period from 1 May 2011, the date on which the 2008 Act became effective -

- (i) the person has been a director of more than one company, or a managing member of more than one close corporation, irrespective of whether concurrently, sequentially or at unrelated times; and
- (ii) during the time that the person was a director of each such company or managing member of each such close corporation, two or more of those companies or close corporations each failed to fully pay all of its creditors or meet all of its obligations, except in terms of-
  - (aa) a business rescue plan resulting from a resolution of the board in terms of section 129 of the 2008 Act; or
  - (bb) a compromise with creditors in terms of section 155 of the 2008 Act.

The section is aimed at protecting the public against people who are involved in the management of several companies and close corporations that were unsuccessful, implicating

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<sup>24</sup> This test is defined in s 4 of the 2008 Act. For a more detailed discussion of the test and its application, see Jean J du Plessis, ‘Company law developments in South Africa: Modernisation and some salient features of the Companies Act 71 of 2008’ (2012) 27 *Australian Journal of Corporate Law* 46 at 55-65.

<sup>25</sup> See s 76 (Standards of director conduct) of the 2008 Act.

that these individuals are not competent and pose a risk to the public and creditors.<sup>26</sup> The courts have, to date, not given probation orders and it is uncertain how this will operate in practice: Will the director under probation still have powers as director; or will the director exercise any powers under the supervision of the person under whose probation he/she operates? It may be that the relationship will be the same or the equivalent of the business rescue practitioner vis-à-vis the board of the company that is under business rescue.<sup>27</sup>

#### **4 Conditions attached to delinquency and probation orders**

The possibility that some conditions can be attached to delinquency and probation orders, are contained in section 162(10) of the 2008 Act:

Without limiting the powers of the court, a court may order, as conditions applicable or ancillary to a declaration of delinquency or probation, that the person concerned-

- (a) undertake a designated programme of remedial education relevant to the nature of the person's conduct as director;<sup>28</sup>
- (b) carry out a designated programme of community service;
- (c) pay compensation to any person adversely affected by the person's conduct as a director, to the extent that such a victim does not otherwise have a legal basis to claim compensation;<sup>29</sup> or
- (d) in the case of an order of probation-

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<sup>26</sup> This provision is aimed at the 'phoenix' companies, where a director of a company that is liquidated due to commercial insolvency merely starts a new company and repeats the process many times.

<sup>27</sup> The analogy is based on s 137(2) of the 2008 Act. See further *Prinsloo and Others v S* [2016] 1 All SA 390 (SCA) para 46, where the Supreme Court of Appeal accepted that the ordinary meaning of 'manage' is 'to be in charge of or to run'.

<sup>28</sup> In terms of s 171(2) of the 2008 Act the Commission can also issue 'compliance notices' under the circumstances as provided for in s 171(1) which could have a similar effect as the conditions for remedial education. The first such compliance notice was issued on 31 March 2015 and required, *inter alia* that: '\*Mr [X] to attend a corporate governance and a director duties course within 90 business days from the date of the Compliance Notice; ...'.

<sup>29</sup> This could, for example, include employees in that capacity and not in the capacity of creditors and could also apply to creditors and, it is submitted, certain distributions to shareholders such as a fixed dividend. The compensation can be ordered even if the company is not in liquidation. It should be noted that creditors have additional rights against, usually, directors in the case of a winding-up of a company unable to pay its debts: see s 424 of Chapter XIV of the 1973 Companies Act that still applies due to the provisions of Item 5(7) of Schedule 5 of the 2008 Companies Act. Whether 'compensation' here would be the same as damages is doubted, as in many instances, such as in the case of a shareholder or employee, there may not be damages in the legal sense of the word, either delictual or contractual.



- (i) be supervised by a mentor in any future participation as a director while the order remains in force; or
- (ii) be limited to serving as a director of a private company, or of a company of which that person is the sole shareholder.

These provisions provide ways of guiding individuals under probation to be able to act as directors again. The proposed conditions, such as the programme of remedial education, are not defined and it is uncertain how this will be implemented in practice. It should also be noted that there is no minimum requirement in respect of the qualifications or education or skill that a director of a company needs.<sup>30</sup> The proposed ‘designated programme of remedial education’ will, at the least have certain minimum requirements. What these will be will obviously depend on the circumstances, but in this context it is submitted that the minimum that will be required is education in respect of ‘skill’ as provided for in section 76(3)(c), as it is doubted if fiduciary duties in general or care and diligence in particular can or should be taught, and if so, by whom. Section 162(1)(d)(ii) also makes provision that a person can be limited to serving as a director of a private company, or of a company of which that person is the sole shareholder. The impression is created that the possible prejudice to third parties in a private company may be limited and that the proportional prejudice will be less. This is, however, not the case. In *Bernstein and Others v Bester and Others*<sup>31</sup> the Constitutional Court emphasised the role of the company:

[t]he establishment of a company as a vehicle for conducting business on the basis of limited liability is not a private matter. It draws on a legal framework endorsed by the community and operates through the mobilisation of funds belonging to members of that community. Any person engaging in these activities should expect that the benefits inherent in this creature of statute will have concomitant responsibilities. These include, amongst others, the statutory obligations of proper disclosure and accountability to shareholders.<sup>32</sup>

The second possibility, to allow such a person under probation to be a director of a company of which that person is the sole shareholder, is, also in light of the *dictum* in the *Bernstein* case,

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<sup>30</sup> See eg *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W).

<sup>31</sup> 1996 (2) SA 751 (CC).

<sup>32</sup> *Ibid* para 85.

even more illogical. The 2008 Act had, before the amendment by the Companies Amendment Act 3 of 2011, the following provision in section 69:

- (12) Despite being disqualified in terms of subsection (8)(b)(iii) or (iv), as a consequence of a single conviction or loss of office as, the case may be, a person may act as a director of a private company if all of the issued securities shares of that company are held by that disqualified person alone, or by—
- (a) that disqualified person; and
  - (b) persons related to that disqualified person, and each such person has consented in writing to that person being a director of the company.

This provision was, however, deleted by section 46(c) of the Companies Amendment Act 3 of 2011 as the commentary on it was that it exposed persons dealing with companies to unacceptable risks. It would seem that the second part of section 162(1)(d)(ii) should also have been deleted due to the deletion of section 69(12), but this was not done. The present wording of the second part of section 162(1)(d)(ii) indeed exposes the third parties to risks that may not be proportional to the aim of that provision. To allow a person under probation to serve as a director of a private company, or of a company (public or private) of which that person is the sole shareholder disregards the function and role of a company, as also stated in the *Bernstein* case *supra*. Any company would, at least to some extent, have outside stakeholders such as creditors and/or employees, and these creditors and/or employees are then at the mercy of a company that is under control of a person who is, arguably, not fit to manage that company. The fact that the company may also have employees exacerbates the possibility of abuse and prejudice. To require the person under probation to hold all the shares, thereby implying that the particular person bears all the risk is not logical. Also the restriction is on 100% shareholding, but there is no reference to securities. All shares are securities, but not all securities are shares, as section 1 of the 2008 Act defines securities as ‘...any shares, debentures or other instruments, irrespective of their form or title, issued or authorised to be issued by a profit company.’ Therefore, although a person holds all the shares, there may be, and the company will be able to issue, securities other than shares, such as debentures.<sup>33</sup> The Commission must establish and maintain a public register of persons who are disqualified from serving as a director, or who are subject to an order of probation as a director, in terms of an

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<sup>33</sup> See s 43 of the 2008 Act.

order of a court pursuant to the 2008 Act or any other law,<sup>34</sup> which may protect the new investor or creditor or employee through the disclosure, but the existing categories of those persons will not be so protected.

## **5 Periods of being declared a ‘delinquent’ or ‘under probation’**

### **5.1 Delinquency**

The different periods for which a person can be declared to be a delinquent person are also quite unique. The first category of such declarations apply ‘for the lifetime of the person declared delinquent’ – that is the equivalent to a lifetime sentence of imprisonment and these persons do not have the right to apply for this order to be suspended or set aside,<sup>35</sup> which seems quite drastic. These cases are, however, limited to cases where a person was already automatically disqualified, including having been declared a delinquent director, but in defiance of this disqualification acted as a director, prescribed director or managing member of a close corporation.<sup>36</sup> The *minimum number of years* the court can order a person as delinquent director is *seven years* from the date the order is made.<sup>37</sup> It is, however, in the court’s discretion to make an order for a person to be declared a delinquent director for a period *longer* than seven years.<sup>38</sup>

### **5.2 Under probation**

The maximum period a person could be placed under probation is five years.<sup>39</sup>

## **6 Application to suspend delinquency and probation orders**

Except for a person who was disqualified for a lifetime because he or she acted as director or managing member of a close corporation while disqualified,<sup>40</sup> others declared delinquent can, at any time more than three years after the order of delinquency was made, apply to a court for the suspension of the order of delinquency and for such an order to be substituted with an order of probation, which may or may not contain conditions.<sup>41</sup> This is another fascinating provision where a person apply to a court to be put under a different order and one wonders whether the

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<sup>34</sup> See s 162(13) of the 2008 Act.

<sup>35</sup> S 162(11) read with s 162(6)(a) and s 162(5)(a) and (b) of the 2008 Act.

<sup>36</sup> Again s 162(11) read with s 162(6)(a) and s 162(5)(a) and (b) of the 2008 Act.

<sup>37</sup> S 162(6)(ii) of the 2008 Act and see discussion under Part 8.

<sup>38</sup> This is also provided for in s 162(6)(ii) of the 2008 Act.

<sup>39</sup> S 162(9)(b) of the 2008 Act.

<sup>40</sup> See again s 162(6) read with s 162(5)(a) or (b) of the 2008 Act.

<sup>41</sup> S 162(11)(a) of the 2008 Act.

person will then request the court to make an unconditional order or make suggestions to the court what conditions should be linked to such a probation order. Linked to the last-mentioned substitution, the person (now only under a probation order), may apply to a court for the setting aside of such probation order (the one that substituted the order of delinquency), but only after two years after the order of delinquency was suspended.<sup>42</sup> A person under a probation order (contrasted with a delinquency order) can only apply to a court for the setting aside of such an order after two years after such an order was made.<sup>43</sup> Again the complexity of these provisions will be apparent.

With reference to the application of substitution or suspension explained above, section 162(12) of the 2008 Act provides as follows:

On considering an application contemplated in subsection (11), the court may-

- (a) not grant the order applied for unless the applicant has satisfied any conditions that were attached to the original order, or imposed in terms of subsection (11)(a); and
- (b) grant an order if, having regard to the circumstances leading to the original order, and the conduct of the applicant in the ensuing period, the court is satisfied that-
  - (i) the applicant has demonstrated satisfactory progress towards rehabilitation, and
  - (ii) there is a reasonable prospect that the applicant would be able to serve successfully as a director of a company in the future.

The idea of ‘rehabilitation’ and the fact that the court must consider whether there is a ‘reasonable prospect’ for the person ‘to serve successfully as a director of a company in the future’ are quite novel. Views may differ whether it is really possible to determine what is meant by ‘rehabilitation’ in this context. The notion of a ‘reasonable prospect’ was defined, in the context of business rescues, as follows:

As a starting point, it is generally accepted that it is a lesser requirement than the ‘reasonable probability’ which was the yardstick for placing a company under judicial

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<sup>42</sup> S 162(11)(b)(i) of the 2008 Act.

<sup>43</sup> S 162(11)(b)(ii) of the 2008 Act.

management in terms of section 427(1) of the 1973 Companies Act (see for example *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pty) Ltd* 2012 (2) SA 423 (WCC) at paragraph [21]). On the other hand, I believe it requires more than a mere *prima facie* case or an arguable possibility. Of even greater significance, I think, is that it must be a reasonable prospect – with the emphasis on ‘reasonable’ – which means that it must be a prospect based on reasonable grounds. A mere speculative suggestion is not enough.<sup>44</sup>

If a person was disqualified from being a director of all companies due to the seriousness of the delinquency, it will be difficult to present a *prima facie* case that there is a reasonable prospect (possibility) that the person will serve successfully as a director in the future. If the person was not disqualified from being a director of all companies, but was a director, with others, on certain company boards, the *prima facie* case will be as difficult, because now the director’s action on those boards must be individualised.

The same principles will apply to the question of ‘rehabilitation’. This sounds like a criminal law issue, and if the director was disqualified because she for example did not hold general meetings or keep proper books,<sup>45</sup> how will the court be convinced that such a person has been ‘rehabilitated’? The discretion should be exercised based on some basic norm or standard, and as was pointed out above, there is no such norm or standard for the appointment of directors or for a person to act as a director and for the courts to determine such a norm or standard would, it is submitted, have the effect that minimum standard/s are created, something that was never part of company law.<sup>46</sup>

## **7 Judicial application of section 162 of the 2008 Act**

### **7.1 *Kukama v Lobelo***

*Kukama v Lobelo*<sup>47</sup> was the first reported case on section 162. The facts were that K and L were equal shareholders in two companies, P (Pty) Ltd and D (Pty) Ltd. Both were directors of P (Pty) Ltd but only L was director of D (Pty) Ltd, but he ‘acted as’ sole and *de facto* director also of P (Pty) Ltd. The SARS paid two amounts, as tax refunds, to D (Pty) Ltd but one tax

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<sup>44</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* [2013] 3 All SA 303 (SCA) para 29 per Brand JA. The court *a quo* also referred to a ‘reasonable possibility’: *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2012 (3) SA 273 (GSJ) para 18.

<sup>45</sup> As was the case in *Msimang NO and Another v Katuliiba and Others* [2013] JOL 29907 (GSJ).

<sup>46</sup> See discussion in Part 4 above.

<sup>47</sup> (38587/2011) [2012] ZAGPJHC 60 (12 April 2012); confirmed on appeal: [2013] ZAGPJHC 72 (31 May 2013).

refund was fraudulently obtained. The refund/s were paid, on instruction of L, to D (Pty) Ltd, which was not entitled to the refund/s and L utilised the refund to make payments that were not for the benefit of P (Pty) Ltd, the company entitled to the refund to a third company T (Pty) Ltd. When L's shareholding in T ceased, he also resigned a director of P (Pty) Ltd.

K applied for an order to declare L delinquent on the grounds that section 76(2)(b) of the 2008 Act creates a duty on the part of a director to communicate at the earliest practicable opportunity any information that comes to his attention to his board. L did not disclose the fact that there was a fraudulent claim made to SARS on behalf of the company and that the other refund payment was made to a different company. The effect of the first respondent's failure to refund SARS the R39m fraudulent claim caused irreparable harm to P (Pty) Ltd as envisaged in section 162(5)(c)(iii) of the 2008 Act. It also exposed P (Pty) Ltd and K to criminal liability as envisaged in section 332(1) and (2) of the Criminal Procedure Act 51 of 1977. By utilising the funds destined for P (Pty) Ltd for the benefit of other companies who are not subsidiaries of P (Pty) Ltd, L also inflicted harm upon P (Pty) Ltd in terms of section 162(5)(c)(iii) of the 2008 Act and in breach of the fiduciary duties he owed to the P (Pty) Ltd.

By failing to detect the fraud to SARS, the conduct of L amounted to gross negligence, and by failing to pay it back to SARS and/or to the account that it should have been paid into initially as required by the loan agreement between Firstrand Bank Ltd and P (Pty) Ltd, L's conduct amounted to wilful misconduct or breach of trust as envisaged in section 162(5)(c)(iv)(aa) and (bb) of the 2008 Act.

The court granted the application because L's conduct fell short of the standard expected of a director of P (Pty) Ltd to such an extent that it amounts to wilful misconduct, breach of trust and a gross abuse of his position as a director. L was grossly negligent in failing to detect the SARS fraud and in not suspecting 'fowl' (sic) play. L's gross negligence inflicted harm upon P (Pty) Ltd and exposed it to unnecessary litigation and to criminal liability. In addition, L should not have paid the amount to the various entities that he had paid to from D (Pty) Ltd's account, but should have transferred the refund into the P (Pty) Ltd's account and dealt with it in consultation with his co-director and shareholder from that account.

Notwithstanding the strained relationship between K and L as both directors and shareholders of P (Pty) Ltd and D (Pty) Ltd, the Court said that the legal obligations of a director bound L to discharge his duties in the same manner that it should, had the relationship between the two been normal.

An order declaring a director delinquent does not also require an order for the removal of the director due to the ‘automatic inherent effect’ of such a declaration.<sup>48</sup> The ‘automatic inherent effect’ of the order is, however, not as clear. Section 69(4) of the 2008 Act provides that a person who becomes ineligible or disqualified while serving as a director of a company ceases to be *entitled to continue to act* as a director immediately,<sup>49</sup> subject to section 70(2), while section 69(8)(a) provides that a person becomes so disqualified if the Court has declared the person to be delinquent in terms of section 162. What section 69(4) states is that the person does not vacate the office immediately. Section 70(1) then states that a person ceases to be a director and a vacancy arises on the board, if that person becomes ineligible or disqualified in terms of section 69. It would therefore seem that if the Court gives an order of delinquency, the person first ceases to be *entitled to continue to act* as a director, and then ceases to be a director. These are curious circuitous provisions.<sup>50</sup> If a Court, such as in *Kukama v Lobelo* declares a director delinquent, and that director vacates her office, and the Memorandum of Incorporation provides that there should be two directors elected by shareholders, it will lead to the situation that the company does not, at least until the new election, a valid board.

## **7.2 *Gihwala and Others v Grancy Property Ltd and Others***

The delinquency provisions were also subject to a judgment by the Supreme Court of Appeal in *Gihwala and Others v Grancy Property Ltd and Others* (‘*Gihwala SCA case*’)<sup>51</sup> on appeal from *Grancy Property Limited and Another v Gihwala and Others; In Re: Grancy Property Limited and Another v Gihwala and Others* (‘*Grancy a quo case*’).<sup>52</sup> G and M were directors and shareholders of SMI (Pty) Ltd (‘SMI’). M acquired shares in SMI through Grancy (Pty) Ltd. This was not an ordinary corporate shareholding structure as it was agreed, albeit it tacitly, that in the management of M’s investment G, M, the trust controlled by G and SMI owed Grancy a duty to exercise good faith and to account fully for their stewardship of Grancy’s investment. Their relationship with Grancy was a fiduciary one<sup>53</sup> and Grancy was not merely a shareholder in SMI – the relationship was an investment agreement underpinned by confidence, trust and good faith<sup>54</sup>. In this respect it should be noted that the directors were

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<sup>48</sup> Para 21.

<sup>49</sup> The words in italics were inserted by the Companies Amendment Act 3 of 2011.

<sup>50</sup> See Piet Delport, *Henochsberg on the Companies Act 71 of 2008*, Loose Leave Service (2016) 263 for a discussion of ss 69, 70 and 71.

<sup>51</sup> [2016] 2 All SA 649 (SCA).

<sup>52</sup> (1961/10; 12193/11) [2014] ZAWCHC 97 (26 June 2014)

<sup>53</sup> Para 58.

<sup>54</sup> *Grancy a quo case* para 19.

therefore, in that capacity, acting in more than one capacity. In the first instance they were acting for SMI based on the ‘fiduciary relationship’ between SMI and Grancy, but also, in the second instance as directors of SMI purely in that capacity. Non-compliance with the fiduciary relationship would entail a breach by SMI and remedies should be based on that basis, which would not necessarily include 162 remedies. However, if the director in that capacity contravened section 162(5), it would lead to the actions and remedies in terms of section 162.

## **8 Constitutionality of section 162 challenged**

### **8.1 Background**

The constitutionality of section 162 was challenged by G and M on the grounds *inter alia* that it operated retrospectively and that it was overbroad. The *Grancy a quo* case and the *Gihwala SCA* case made important comments about the ambit and purpose of section 162 in discussing whether it is in accordance with the Constitution of the Republic of South Africa 108 of 1996.<sup>55</sup> It was contended in the *Grancy a quo* case that section 162 imposes a *post facto* punitive regime that restricts directors’ rights to practise their chosen trade or occupation and thus violates the rule of law.<sup>56</sup> In that case the Court, however, said that it is a civil remedy in respect of conduct which was also unlawful under the 1973 Act.<sup>57</sup> The subjective position of an applicant is irrelevant to the determination of the validity of a statutory provision, and such validity must be determined objectively. However, in the *Grancy a quo* case the Court said that although the constitutional validity of a statutory provision is determined objectively,<sup>58</sup> the applicants cannot challenge the validity of those parts of section 162 that are not applicable to them,<sup>59</sup> and the finding of the Court in respect of constitutionality therefore only applies to the provisions of section 162(5) of the 2008 Act.

In respect of retrospectivity, Item 7(7) of Schedule 5 of the 2008 Act provides that any right of a person to seek a remedy in terms of the 2008 Act applies with respect to conduct pertaining to a pre-existing company<sup>60</sup> and occurring before the effective date,<sup>61</sup> unless that person

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<sup>55</sup> ‘Constitution’. The *Gihwala SCA* case rejected the appeal from the *Grancy a quo* case in respect of the constitutional challenge in respect of s 162(5)(c) read with s 162 (6)(b).

<sup>56</sup> Para 151.3.

<sup>57</sup> Para 175.

<sup>58</sup> *De Reuck v DPP*, WLD 2004 (1) SA 406 (CC) para 85.

<sup>59</sup> Section 38 (a) of the Constitution and *Poswa v MEC for Economic Affairs, Environment and Tourism, Eastern Cape* 2001 (3) SA 582 (SCA) paras 21-22.

<sup>60</sup> As defined in s 1 as a company that existed before the 2008 Act came into operation.

<sup>61</sup> The effective date in terms of s 1 is the date on which a provision of the 2008 Act came into operation in terms of s 225 of the 2008 Act. Section 225 provides that the 2008 Act comes into operation on a date fixed by the



commenced proceedings in a court in respect of the same conduct before the effective date.<sup>62</sup> In the *Grancy a quo* case the Court said that the wording of item 7(7) of Schedule 5 is unambiguous and its meaning is clear, namely, that, in an application under section 162 of the 2008 Act, past conduct of the relevant director may be taken into account, unless proceedings in respect thereof had already been commenced before the effective date. Item 7(7) of Schedule 5 therefore does not create true retrospectivity, it attaches prospective consequences to previously unlawful conduct in the interest of protecting the public and maintaining appropriate standards of corporate governance. Such an interpretation does not, in the opinion of the Court *a quo*, lead to any absurdity.<sup>63</sup> In the *Gihwala* SCA case the same conclusion was reached, but also based on the established principle of our law that a statute is not retrospective merely ‘because a part of the requisites for its action is drawn from time antecedent to its passing’, and the Supreme Court of Appeal opined<sup>64</sup> that this is actually all that item 7(7) in Schedule 5 to the 2008 Act provides.<sup>65</sup>

In deciding whether the ‘retrospective’ application of section 162(5)(c) is inconsistent with rule of law and right to equality, it is, according to the *Grancy a quo* case, required to compare the 2008 and 1973 Acts.<sup>66</sup> Section 162 of the 2008 Act provides for a civil remedy for conduct which was unlawful under 1973 Act<sup>67</sup> and the conduct under section 162(5)(c) was also covered under section 219 of the 1973 Act. In addition, there was no minimum or maximum periods of removal in terms of the 1973 Act, but the director could apply for an order setting aside the declaration at any time, while section 162 sets a minimum disqualification of 7 years, but the director can apply for suspension of the order or for the order to be substituted for probation after 3 years. Under section 219 the order was for any involvement in the management of a company, while section 162 provides for a disqualification only as director or prescribed officer. It was also stated in the *Gihwala* SCA case that in addition,

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President by proclamation in the Government Gazette, which was 1 May 2011 according to R 32 of 2011 as published in Government Gazette 34239 of 19 April 2011.

<sup>62</sup> The application of Item 7(5) in conjunction with Item 7(7) in Schedule 5 to the 2008 Act as in *Msimang NO and Another v Katuliiba and Others* [2013] JOL 29907 (GSJ) was with respect not correct: See Piet Delpont, *Henochsberg on the Companies Act 71 of 2008*, Loose Leave Service (2016) 564.

<sup>63</sup> *Grancy a quo* case paras 163 and 164.

<sup>64</sup> Para 141.

<sup>65</sup> *Krok and another v Commissioner, South African Revenue Service* [2015] ZASCA 107; 2015 (6) SA 317 (SCA) para 40. This is all that item 7(7) in Schedule 5 to the 2008 Act provides.

<sup>66</sup> Para 170.

<sup>67</sup> Para 175.

disqualification in terms of section 162 could be restricted to a particular category of company.<sup>68</sup> As such the effect of section 162 is not as harsh as that of section 219.

The effect of section 162, for purposes of the constitutional challenge, must also be evaluated against the background and purposes of the 2008 Act. The Court *a quo* referred to the Policy paper<sup>69</sup> and the Memorandum on the Objects of the Companies Bill 2008,<sup>70</sup> and stated<sup>71</sup> that section 162 was introduced with the following objectives:<sup>72</sup>

154.1 A need was identified for greater protection of the public and investors against the conduct of unscrupulous company directors. Such directors are to be eliminated, not only to prevent losses to investors, but also to boost confidence in the South African Regulatory System in order to attract investment and stimulate growth.

154.2 In order to achieve the objectives, it was necessary, in the first place, to define the rights, duties and obligations of directors in the 2008 Act itself, and not rely on ill-defined common law rights, duties and obligations.

154.3 It was further necessary to provide an effective enforcement mechanism for those harmed by the conduct of rogue directors. The threat of criminal prosecution proved to be an ineffective deterrent. It became necessary to add an array of administrative and civil remedies to the 2008 Act, aimed at deterring directors from abusing their office and eliminating those found guilty of improper conduct from operating in South Africa.

The civil remedy as in section 162 is a remedy as envisaged as in para 154.3.<sup>73</sup>

## **8.2 Constitutionality: *Grancy a quo* case**

The contention was that the provisions of section 162(5)(c) were ‘unconstitutional’, *inter alia*, because infringes on the separation of powers, that it is overbroad in that it does not give the Court a discretion to declare a director delinquent (due to the imperative ‘must’ in section 162(1)) (paras 185 and 186) and that it infringes on the constitutional rights to professional freedom (section 22 of the Constitution) and human dignity (see 10 of the Constitution). In

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<sup>68</sup> Para 144.

<sup>69</sup> GG 26493 of 23 June 20014.

<sup>70</sup> The final Bill that resulted in the 2008 Act, which differed substantially from the original Bill of 2008, did not contain such a memorandum.

<sup>71</sup> Para 154.

<sup>72</sup> See also *Westinghouse Brake and Equipment (Pty) Ltd v Bilger Engineering (Pty) Ltd* 1986 (2) SA 555 (A) in respect of the use of an official report preceding an Act to determine the purpose of the 2008 Act.

<sup>73</sup> Court *a quo* para 155.

respect of the separation of powers, the issue is whether there is sufficient discretion, with reference to the Bill of Rights,<sup>74</sup> which in this instance were sections 22 and 10 of the Constitution. The Court found that section 162(5)(c) regulates the right to practice the profession of a director,<sup>75</sup> and the only question is whether such regulation is rational<sup>76</sup> and whether it is rational to eliminate a person from serving as director for a period of time. The Court found that the elimination of a person due to conduct that is serious misconduct constituting gross abuses of the position of director is not irrational and that section 162(5)(c) is rationally related to its objectives.<sup>77</sup> The second challenge was that the period of delinquency is not in the discretion of the Court, and whether this is rational. This the Court found to be the case as the 7 year period can, under certain circumstances, ameliorated to 3 years. Also, a minimum prescribed period will ensure consistency in the application of section 162 and also ensure that the section has a sufficient deterrent effect.<sup>78</sup> The right to dignity is not infringed in the removal of a director because of delinquency, and the Court therefore found that section 163(5)(c) was not unconstitutional.<sup>79</sup>

### **8.3 Constitutionality: *Gihwala* SCA case**

In the *Gihwala* SCA case the issues were that absence of flexibility in regard to imposition of delinquency infringes constitutional rights to dignity (section 10 of the Constitution), trade occupation or profession (section 22 of the Constitution) and access to courts (section 34 of the Constitution),<sup>80</sup> but that focus was on the right to dignity.<sup>81</sup>

The purpose of section 162 was to protect the investing public, whether sophisticated or unsophisticated, against the type of conduct that leads to an order of delinquency, and in effect to protect those who deal with companies against the delinquent conduct of directors. As authority for this statement the Supreme Court of Appeal referred to *Re Gold Coast Holdings Pty Ltd (In Liq); Australian Securities & Investments Commission v Papotto*.<sup>82</sup> However, this

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<sup>74</sup> Para 187.

<sup>75</sup> The *Gihwala* SCA case para 146 said that in respect of the application of s 22 of the Constitution, the correctness of the proposition that being a director of companies is an ‘occupation, trade or profession’, is by no means obvious.

<sup>76</sup> Para 188.

<sup>77</sup> Paras 190-191.

<sup>78</sup> Paras 193-194.

<sup>79</sup> Paras 197-199.

<sup>80</sup> The SCA found that the Court was involved in all of the s 162 procedures and it is therefore not an infringement of s 34.

<sup>81</sup> Para 141.

<sup>82</sup> [2000] WASAC 201 para 22.

case, deals with legislation comparable to section 219 of the 1973 Companies Act and does not relate to deal with issues in respect of comparable to section 162 of the 2008 Act.

In the *Gihwala SCA* case the Supreme Court of Appeal, in discussing the standard of fault, recklessness or gross negligence that would trigger section 162, made the point

that there was a complaint that gross negligence could trigger a delinquency order. There is no merit in this complaint. There is a long history of courts treating gross negligence as the equivalent of recklessness, when dealing with the conduct of those responsible for the administration of companies, and recklessness is plainly serious misconduct. It was urged upon us that there might be circumstances of extenuation, or perhaps that, notwithstanding the seriousness of the conduct, the company might not have suffered any loss.<sup>83</sup>

However, these considerations are not relevant to the protective purpose of the section. The aim of section 162 was:

... to ensure that those who invest in companies, big or small, are protected against directors who engage in serious misconduct of the type described in these sections. That is conduct that breaches the bond of trust that shareholders have in the people they appoint to the board of directors. Directors who show themselves unworthy of that trust are declared delinquent and excluded from the office of director. It protects those who deal with companies by seeking to ensure that the management of those companies is in fit hands. And it is required in the public interest that those who enjoy the benefits of incorporation and limited liability should not abuse their position.<sup>84</sup>

However, only gross abuses of the position of director, such as stated in section 162(5)(c), qualify.<sup>85</sup> The provision was not attacked on the basis of irrationality, but the requirement remains that there must be a rational connection between the purpose of the legislation and the provision under consideration. 'Patently it is an appropriate and proportionate response by the Legislature to the problem of delinquent directors and the harm they may cause to the public who place their trust in them.... Rationality is the touchstone of legislative validity and section 162(5)(c), read with section 162(6)(b)(ii), is rational.'<sup>86</sup>

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<sup>83</sup> Para 144.

<sup>84</sup> Para 144.

<sup>85</sup> Para 143.

<sup>86</sup> Para 145.

In terms of section 22 of the Constitution every citizen has the right to choose their trade, occupation or profession freely but the practice of a trade, occupation or profession may be regulated by law, as long as ‘it is in the public interest and not arbitrary or capricious, regulation of vocational activity for the protection[,] both of the persons involved in it[,] and of the community at large affected by it[,] is to be both expected and welcomed.’<sup>87</sup> These seems to be sensible and realistic qualifications to the constitutional rights of individuals. It would be unacceptable if the public interest should be compromised based on individual interests of alleged individual constitutional rights.

The Supreme Court of Appeal said that even if it is assumed that being a director of companies is an occupation, trade or profession, a proposition the correctness of which is by no means obvious, it was not suggested that section 162(5) is either capricious or arbitrary and on that ground alone, the constitutional challenge based on section 22 of the Constitution must fail.<sup>88</sup>

It was contended by the appellants that the constitutional right to dignity (section 10 of the Constitution) is infringed because section 162 does not permit the Court to take into account the director’s circumstances and degree of blameworthiness. It is therefore a question of appropriateness of the protective measures that the legislature has prescribed to deal with delinquent directors, bearing in mind that only serious misconduct results in delinquency. This is merely an attack on the rationality of the provision that an order of delinquency *must* be given by the Court if the conduct as in section 162(5)(c) is proved. No case was made out that it is irrational, and therefore it cannot be unconstitutional.<sup>89</sup>

#### **8.4 *Foss v Harbottle***

The rule in *Foss v Harbottle*<sup>90</sup> was used in the *Grancy a quo* case a basis why the application for delinquency must fail. In the appeal the *Gihwala SCA* case referred to this as: ‘It is a curious feature of this case that we are asked to apply a rule, or more accurately a combination of rules, of ancient origin that has been abolished in the country of its birth.’<sup>91</sup> It is not intended to discuss the rule here, but the following summary of the rule is, with respect, helpful to demystify it: ‘It precludes shareholders from suing in their own right where the claim is one in respect of a wrong done to the company causing it to suffer loss. That is so even where the

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<sup>87</sup> *Affordable Medicines Trust and others v Minister of Health of RSA and others* 2006 (3) SA 247 (CC) paras 57–60.

<sup>88</sup> Para 146.

<sup>89</sup> Paras 149-150. Paras 149-150.

<sup>90</sup> (1843) 2 Hare 461; 67 ER 189.

<sup>91</sup> Para 107.

result is to diminish the value of the shareholder's shares or deprive them of a dividend and the company has declined or failed to take steps to recover the loss. On the other hand, where there is no wrong to the company, but only one to the shareholder, there is no reason to bar the shareholder from suing. That is so even if the measure of the shareholder's loss is the diminution in value of their shareholding.<sup>92</sup> The third part of the rule, as stated in *Johnson v Gore Wood & Co (a firm)*<sup>93</sup> is that:

Where a company suffers loss caused by a breach of duty to it, and a shareholder suffers loss separate and distinct from that suffered by the company caused by a breach of duty independently owed to the shareholder, each may sue to recover the loss caused to it by breach of the duty owed to it but neither may recover loss caused to the other by breach of the duty owed to that other.<sup>94</sup>

In respect of shareholders' rights,<sup>95</sup> section 162 does not fall within either of the categories above and in that sense it is submitted that it is a *sui generis* rule. This is the case because although the misconduct that can put the section in operation is in respect of duties towards the company, a shareholder has direct access to section 162, and this access is not subject to inaction by the company itself, and the injustice is not required to in respect of the shareholders' rights. The protection of the shareholder is, as stated in the *Gihwala SCA* case to protect the shareholder from unscrupulous directors acting as such vis-à-vis the company.<sup>96</sup> This is a new direction in the 2008 Act, and is also apparent in other *sui generis* shareholder (and stakeholder) rights, irrespective whether the duties are owed to them directly.<sup>97</sup>

## **9 Conclusion**

There were significant reforms regarding the disqualification of company directors under the 2008 Act as far as declaring persons 'delinquent director' or placing a person under 'probation'. 'Delinquent directors' are disqualified from acting as directors, whereas a person under 'probation' may still act as director, but only under the conditions stipulated by the Court under sections 162(9). In addition, the Court can, under section 162(10) stipulate conditions for both delinquent directors or directors under probation to undertake designated programmes and

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<sup>92</sup> Para 109.

<sup>93</sup> [2001] 1 All ER 481 (HL) at 503

<sup>94</sup> As quoted in para 110. The *dictum* is obviously subject to the provisions of s 165(1) of the 2008 Act, which abolishes the common law derivative action.

<sup>95</sup> Section 162 can be invoked by persons other than shareholders: see s 162(3) and (4) and discussion Part 2 *supra*.

<sup>96</sup> Para 144.

<sup>97</sup> See eg s 20(6) of the 2008 Act.

community service as well as pay compensation to persons affected by their conduct. The periods for which persons could be declared delinquents or under probation vary. The maximum period a person could be placed under probation is five years. There is no maximum period a court could declare a person to be a delinquent director. However, the minimum period for a delinquency order is three years.

Unique provisions apply to applications to suspend or substitute delinquency orders. A delinquency order could, for instance, be substituted with a probation order and it can be assumed that the Court may again stipulate conditions or make ancillary orders relating to such a probation order.

It is clear from the cases that courts are cognisant of the potential harm that directors acting in a delinquent manner can cause loss to the investor, be it a creditor or shareholder of a company and the courts do not shy away from delinquency orders. On the other hand it is also clear that delinquency orders are not a last resort remedy. Therefore a shareholder apparently does not need to prove that other remedies, including a compliance order by the Commission for example not preparing financial statements, have been exhausted. This may be a too liberal interpretation of the powers to grant delinquency (and probation) orders, but it may also be added that the cases decided have clearly indicated that shareholder remedies would be ineffective. The positive aspect of the delinquency (and probation) orders is that certain remedies, especially for creditors and employees to hold the director/s personally liable, is not subject to winding-up of the company.<sup>98</sup>

There is no doubt that the South African provisions regarding disqualification are unique. Not only for the terminology used like ‘delinquency’ and ‘probation’ linked to the disqualification of directors, but also as far as the procedures stipulated for the application for delinquency and probation orders are concerned. In addition, remedial conditions could be stipulated in probation orders, *inter alia*, to undertake educational and community service programmes.

It is submitted that the core problem of section 162 is its complexity. Different parties have standing to apply for delinquency or probation orders respectively, and the circumstances under which these parties can apply for such orders are also different and require careful interpretation to comprehend. Although the underlying purpose of these provisions by the legislature is

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<sup>98</sup> Shareholders do have remedies under the same circumstances, broadly, as the basis for delinquency orders in terms of s 20(6) of the 2008 Act. In terms of s 20(6) a shareholder has a claim for damages against any person, also the directors, who intentionally, fraudulently or due to gross negligence causes the company to anything inconsistent with the 2008 Act or any limitation in terms of s 20.

commendable, it is unlikely that these provisions will be used to their full potential to achieve the ultimate goals with them, namely the protection shareholders, creditors and the public against delinquent directors and to provide opportunities for some directors to gain experience as directors under Court orders placing them 'under probation'. Especially as far as probation orders are concerned, the ultimate objectives with them are very difficult to achieve through legislation that requires of a Court to determine conditions of the probation. These conditions will of necessity require of a Court to anticipate almost infinite potential conditions to ensure the person under probation do not pose too large a risk for those who are supposed to be protected by probation orders.