

Durham E-Theses

*The Role of Voluntary Corporate Governance Codes
in the Interpretation and Application of the Statutory
and Common Law Duties of the Company Director:
A South African Perspective*

STOOP-KOORNHOF, HELENA,HESTER

How to cite:

STOOP-KOORNHOF, HELENA,HESTER (2020) *The Role of Voluntary Corporate Governance Codes in the Interpretation and Application of the Statutory and Common Law Duties of the Company Director: A South African Perspective*, Durham theses, Durham University. Available at Durham E-Theses Online: <http://etheses.dur.ac.uk/13493/>

Use policy

The full-text may be used and/or reproduced, and given to third parties in any format or medium, without prior permission or charge, for personal research or study, educational, or not-for-profit purposes provided that:

- a full bibliographic reference is made to the original source
- a [link](#) is made to the metadata record in Durham E-Theses
- the full-text is not changed in any way

The full-text must not be sold in any format or medium without the formal permission of the copyright holders.

Please consult the [full Durham E-Theses policy](#) for further details.

The Role of Voluntary Corporate Governance Codes in the
Interpretation and Application of the Statutory and Common
Law Duties of the Company Director: A South African
Perspective

Helena H Stoop

Submitted in Fulfilment for the degree of Doctor of Philosophy (Law)

Law School: Durham University

2019

(Text Excluding Bibliography: 92 913 words)

The Role of Voluntary Corporate Governance Codes in the Interpretation and Application of the Statutory and Common Law Duties of the Company Director: A South African Perspective

Helena H Stoop

It is critical that regulators ensure appropriate regimes to govern juristic persons. Of the many techniques devised to ensure good governance, the self-regulatory Code has proven extremely popular across jurisdictions. This is also the case in South Africa where a self-regulatory Code demands high standards of governance and dictates that the so-called 'independent non-executive director' should be a key custodian of corporate governance. The relationship between the Corporate Governance Code and what can be termed 'black letter law' is not yet clearly established. In the South African context, the courts have been willing to consider the principles that the codes espouse when interpreting legal duties conferred upon directors by the common law and statute. Such a step has far reaching implications for the development of this area of the law. This thesis contributes to the discourse by analysing the legality, and consequences of such an approach. It does so by focusing on the South African context which is submitted to be unique. First, a codified constitutional imperative to develop the South African common law gives local courts greater flexibility and, potentially, a remit that accommodates a more vigorous interpretation. Furthermore, the South African Corporate Governance Code is ambitious in its application and aspirational in its contents - applying not only to listed companies but to all entities and vigorously promoting a stakeholder inclusive approach to company governance. This thesis asks: what are the legal and normative boundaries when interpreting this area of corporate law and attempting to align the two sources of regulation? In answering this question, the thesis will contribute in particular to the state of knowledge of South African company law and the application of Corporate Governance Principles in relation thereto and make suggestions for legislative reform.

(Abstract: 291 words)

CHAPTER 1 – INTRODUCTION

1	Overview	1
2	Historical Synopsis	
	a. The Limited Liability Company and the Board of Director	6
	b. Corporate Governance – The Rise of a Movement	12
3	An overview of the Legal Landscape	
	a. South Africa	17
	b. Jurisdictions Chosen for Analysis	23
4	Overview of Definitions, Concepts, Theories and Debates that Inform the Thesis	27
5	Chapter Overview	30
6	Methodology	
7	Conclusion	35

CHAPTER 2 - THE INDEPENDENT NON-EXECUTIVE DIRECTOR: THE ORIGINS OF THE OFFICE, CURRENT REGULATION AND PERSISTENT CHALLENGES

1	Introduction	38
2	Background	42
3	Definitions and Development	43
	a. General Historic Overview	47
	b. The Non-Executive Director in American Law and Practice	48
	c. The Non-Executive Director in English and European Law and Practice	51
	d. The Non-Executive Director in South African Law and Practice	53
4	Challenges and Criticism	56

5	Conclusion	64
---	------------	----

CHAPTER 3 – THE DUTY OF CARE AND SKILL

1	Introduction and Context	67
2	History and Early Development	70
3	Later and Recent Developments	
	a. The United Kingdom	78
	b. South Africa	82
4	Debate Surrounding the Director’s Duty of Care and Skill	
	a. Practical challenges	87
	b. An Overview of the Academic Debate	90
5	Conclusion	98

CHAPTER 4 – THE DUTY TO ACT IN THE BEST INTERESTS OF THE COMPANY

1	Introduction	100
2	A Phrase with many Meanings	103
	a. Shareholder Value	105
	b. The Stakeholder Approach	111
	c. Enlightened Shareholder Value	115
3	The Duty to Act in the Best Interests of the Company	116
4	The Current Legal Position	
	a. United Kingdom	120
	b. South Africa	125
5	The Potential Impact of the Governance Codes	128
6	Conclusion	134

CHAPTER 5 - COLLISIONS AT THE INTERSECTION: PROCEDURAL, PRACTICAL AND CONSTITUTIONAL CONCERNS

1	Introduction	137
2	From Text to Context	
	a. Relevant Developments in the Law of the Interpretation of Documents	140
	b. Corporate Law Through the Prism of the Bill of Rights	155
	c. The Role of Extrinsic Material in Interpreting Legislation	162
	i. Custom	163
	ii. Similar Provisions in Other Statutes	164
	iii. Surrounding Circumstances	165
	iv. Preceding Discussions or Travaux Preparatoires	166
3	Relevant Statutory Provisions	173
4	Interpreting and Developing the Common Law	180
5	Conclusion	184

CHAPTER 6 - COLLISIONS AT THE INTERSECTION: NORMATIVE DEBATES

1	Introduction	187
2	Theories of the Firm	192
3	A Revolution and its Consequence	
	a. Chronology	198
	b. Agency Costs Theory	205
	c. Nexus-of-Contracts Theory	210
4	Recent Developments and Future Possibilities	215
5	Conclusion	222

CHAPTER 7 – ACCOUNTABILITY AND ENFORCEMENT

1	Introduction	225
2	Regulation & Accountability	
	a. Accountability as a General Concept	227
	b. Comply or Explain and the Governance Codes	229
	c. Statutory Duties and Remedies	
	i. Overview of the applicable remedies	236
	ii. The Derivative Action	241
3	The Business Judgement Rule	245
4	Conclusion	254

CHAPTER 8 - REMARKS IN CONCLUSION	256
--	-----

BIBLIOGRAPHY	266
---------------------	-----

Statement of Copyright:

The copyright of this thesis rests with the author. No quotation from it should be published without the author's prior written consent and information derived from it should be acknowledged.

Acknowledgements

My deepest thanks to my supervisor, Prof Jonathan Mukwiri, who has been nothing short of remarkable. The value of his kindness, patience and insight cannot be measured and I have no doubt that none of this would have come to fruition without it. Thank you also to Mr Chris Riley for encouragement throughout.

My sincere thanks to the Commonwealth Scholarship Commission of the United Kingdom who made this wonderful adventure possible. It has been the most profoundly incredible experience, both personally and professionally, and one that I will treasure for a lifetime.

There is not enough space to thank my husband who embarked on this adventure with me. For standing by my side, for holding my hands high, for anchoring my ambitions and giving wings to my dreams I will thank you always.

My incomparable, remarkable parents, thank you.

Thank you to my family – you were always near despite being so far. And a special thank you to my family in the UK for warming our hearts when the winters were cold.

Thank you to my creator, Father God for every opportunity; for as always it is by grace alone.

Dedication

This work is dedicated to Nicolas and Hanna – as is every other endeavour. You make me new.

CHAPTER 1

INTRODUCTION

In my judgement a potent mixture of recession and scandal is no longer needed to keep corporate governance on the public agenda. There is too great a recognition of its importance for the wealth-creating process for it to fall out of fashion. The process of raising standards of corporate governance should I believe be a continuing one. Our proposals should be seen as a step along the road.¹

1 Overview

The limited liability company has been described as a mere ‘figment of the imagination’² and yet it has shaped society immeasurably. It is a ubiquitous feature of modern commercial life. Corporate citizens employ us, feed us, transport us and entertain us. They spark economic growth, lead scientific development, and allow our joint efforts to amaze us. But companies are fallible. They are often corrupted by power, greed or inefficiency. They face crises and they fail, sometimes leaving devastation in their wake.³ It is against this backdrop that the lawmakers that regulate corporate entities are forced to walk a tightrope - seeking an elusive balance between

¹ Adrian Cadbury ‘Restoring trust and confidence in the corporate system’ (1992) 3(12) *ICCLR* 403, 403.

² Per Walton J, *Northern Counties Securities Ltd v Jackson & Steeple Ltd* [1974] 1 WLR 1133.

³ The examples are too numerous to list. See: William W. Bratton ‘Enron and the Dark Side of Shareholder Value’ (2002) 76 *Tul.L.Rev.* 1275; Stephen Copp, ‘Corporate governance: change, consistency and evolution: Part 1’ (2003) 14(2) *ICCL* 65; Stephen Haswell and Elaine Evans ‘Enron, fair value accounting, and financial crises: a concise history’ (2018) 31(1) *AAAJ* 25; Michael Haynes ‘Rationality, morality and Joel Bakan’s *The Corporation*’ (2007) 3(1) *IJBGE* 1; Jerry W Markam *A Financial History of Modern U.S. Corporate Scandals from Enron to Reform* (Routledge 2006); Rinita Sarker ‘Daiwa and Barings: A Blueprint for Disaster’ (1996) 17 *Co Law* 86; MM Scharff ‘Understanding WorldCom’s accounting fraud: did groupthink play a role?’ (2005) 11(3) *JLOS* 109; Raymonde Crête ‘The Volkswagen Scandal from the Viewpoint of Corporate Governance’ (2016) 7 *EJRR* 25.

accountability and efficiency.⁴ And it is in response to these challenges that many jurisdictions now supplement traditional statutory measures with voluntary Codes of Governance.⁵ These Codes have mostly been self-regulatory and have applied to listed entities only, but recent debates centre around the possible application of the Codes to large private companies,⁶ and in South Africa, judicial precedent has hinted at incorporating the

⁴ As Clarke points out, '[c]ycles of crisis and reform in corporate governance are now a worldwide phenomenon' see Thomas Clarke *International Corporate Governance: A Comparative Approach* (2nd edn Routledge 2017) 1. And more recently in the examples such as: BBC 'Carillion collapse to cost taxpayers £ 148 m' (7 June 2018) available online at <https://www.bbc.co.uk/news/business-44383224> accessed on 18/07/2019; BBC 'Thomas Cook bosses face scrutiny over collapse' (24 September 2019) available online at <https://www.bbc.co.uk/news/business-49805014> accessed on 25/09/2019.

⁵ Almost all developed and developing economies have introduced corporate governance codes while many have also enacted new company laws: Bob Tricker *Corporate Governance: Principles, Policies and Practices* (3rd edn Oxford 2015) 3. Some national examples include: FRC *The UK Corporate Governance Code* (2016), FRC, London available online <www.frc.org.uk/getattachment/ca7e94c4-b9a9-49e2-a824-ad76a322873c/UK-Corporate-Governance-Code-April-2016.pdf>; ASX *Corporate Governance Principles and Recommendations* (2014) ASX, available online <www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-3rd-edn.pdf>; China Securities Regulatory Commission (2001) *Corporate Governance for Listed Companies in China* CSRC, State Economic Trade Commission, Beijing available online <www.ecgi.org/codes/documents/code_en.pdf> There are also several international codes of best practice. See for example: OECD *The OECD Principles of Corporate Governance* (2015) OECD Paris available online <www.oecd.org/corporate/principles-corporate-governance.htm>; The Basle Committee on Banking Supervision (2015) *Corporate Governance Principles for Banks* Bank for International Settlements, Basle; available online <www.bis.org/bcbs/publ/d328.pdf>; ICGN (2014) *ICGN Global Governance Principles* ICGN, London available online <www.ecgi.global/code/icgn-global-governance-principles>. See also in general: Andreas M Fleckner & Klaus J Hopt (eds) *Comparative Corporate Governance: A Functional and International Analysis* (Cambridge UP 2013); Du Plessis JJ and Others *Principles of Contemporary Corporate Governance* (4th edn Cambridge UP 2018).

⁶ Department for Business, Energy, & Industrial Strategy 'Corporate Governance Reform: Greenpaper' [2017],43<www.gov.uk/government/uploads/system/uploads/attachment_data/file/640631/corporate-governance-reform-government-response.pdf> accessed 23 November 2017.

principles and recommendations contained in the South African Governance Code when applying so-called 'black letter law'.⁷

These measures pertain to the regulation of an entity that we know can neither be kicked nor damned, as it is famously (or infamously) without body or soul.⁸ However, the courts have consistently held that it does have a 'directing mind and will', as these words of Lord Denning illustrate:

A company may in many ways be likened to a human body. It has a brain and nerve centre which controls what it does. It also has hands which hold the tools and act in accordance with directions from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such.⁹

Directors thus remain the closest thing to a personification of the companies they serve, and it is no surprise that a fair amount of company law is aimed at regulating those at the helm of the corporate ship. We expect a lot from anyone who dares call himself a company director these days – especially as far as larger and listed entities are concerned.¹⁰ Boards today face demanding and apparently contradictory responsibilities. They must balance

⁷ See below at note 111. The courts in Australia have taken more direct steps in this direction, see for example: S.M. Solaiman 'The landmark James Hardie case in Australia: a wakeup call for non-executive directors' (2013) 34 *Co Law* 180; and see chapter 7 note 39 and sources cited.

⁸ *Northern Counties Securities Ltd v Jackson & Steeple Ltd* [1974] 1 WLR 1133.

⁹ *HL Bolton (Engineering) Co Ltd v TJ Graham and Sons Ltd* [1956] 3 All ER 624. This is also known as the organic theory of company law or the directing mind theory. It has more recently faced criticism *cf* R.J. Wickins and C.A. Ong 'Confusion worse confounded: the end of the directing mind theory?' (1997) *J.B.L* 524.

¹⁰ This is perhaps more true for those serving on boards of companies in the financial sector, where additional rules apply and, for example in the United Kingdom, the Financial Conduct Authority holds significant influence, especially following the introduction of the Senior Managers Regime. See in overview: James McCalman & Angus Young 'Another round of corporate governance reforms in the UK: implications for directors in the financial sector' (2018) 33(8) *J.I.B.L.R* 286.

an entrepreneurial spirit and the need to drive the business forward with the prudent control and an eye on risk. They must remain sufficiently detached to ensure objectivity and a longer-term view, without sacrificing sufficient knowledge of the inner operations of the company to remain accountable for its actions. Increasingly, they have to contend with conflicting interest groups, and ensure that commercial success is not at the cost of employees and other constituents.¹¹

To ensure that directors live up to these high expectations, the law relies largely on several duties that can be divided into two broad categories, with the first comprising a series of obligations anchored in good faith and honesty, and the second an overarching duty to act with care and competence.¹² The system is not fool proof; in fact the legal duties of directors have been labelled ‘...“a confusing and compendious mass of case law and the occasional statutory measure”’.¹³ In addition, practitioners advising clients, and directors themselves, also have to take account of the abovementioned voluntary Corporate Governance Codes that dictate best practice and optimal approaches to management. A key feature of most Governance Codes the world over, is the insistence on several independent non-executive directors to fulfil an overview function and essentially serve

¹¹ Ramani Naidoo *Corporate Governance: An Essential Guide for South African Companies* (2nd edn LexisNexis 2009) 107.

¹² Nolan divides the doctrines into three categories. First, those aimed at defining and limiting the scope of the power that may be exercised; second, techniques that inform the process of decision making; and finally, control mechanisms that address the degree of competence with which the power is exercised. See: R C Nolan ‘Controlling fiduciary power’ (2009) 68(2) *C.L.J.* 293, 294. Davies and Worthington in turn, classify the various duties in relation to the risks faced by shareholders when making an investment. On the one hand the board may be active but may not act in the best interests of shareholders – duties of loyalty speak to this scenario. On the other hand, the board may be slack or incompetent, and duties of care and skill would address such instances. Paul L Davies & Sarah Worthington *Gower’s Principles of Modern Company Law* (Sweet & Maxwell 2016 10th ed) [478], para 16-15. The authors point out that this twofold classification also accords with the two basic common law sources of the rules on directors’ duties.

¹³ L Roach ‘The Legal Model of the Company and the Company Law Review’ (2005) 26 *Co Law* 98.

as a check and balance to managerial discretion.¹⁴ This remains the case although objective voices at board meetings have to date not proven capable of avoiding poor corporate performance and in some instances even wide scale corporate collapses.¹⁵

In the face of this proliferation of Code and statute, we are reminded of Cicero's warning that justice is not the inevitable result of more laws.¹⁶ The question becomes whether the many mechanisms now in place support or undermine one another. This research will consider one part of this broad question - the legal ramifications of an approach that would see voluntary or self-regulatory codes of governance inform the statutory and common law duties of the independent non-executive director through caselaw. The thesis will focus on the position in South African law, but where relevant comparative analysis will refer to best practices in other jurisdictions and international norms and trends with relative emphasis on the position in the United Kingdom. In particular the thesis will ask whether it is legally tenable to draw on the corporate governance code when interpreting statutory provisions and the common law – in other words, is it a sound approach from a constitutional point of view and do the courts have authority to engage with the Code in the manner that they have been doing and, potentially in a

¹⁴ Davies and Worthington (n12) 479. And see Chapter 5 below.

¹⁵ Tricker (n5) 15 – 17, where the author chronicles the cycles of crisis of the early 21st century. The role and responsibilities of the so-called 'non-executive director' has generated much debate. See for example: Baum H 'The Rise of the Independent Director: A Historical and Comparative Perspective' *Max Planck Private Law Research Paper No. 16/20*; A J Boyle 'Company Law and the Non-Executive Director – The USA and Britain Compared' (1978) 27 *ICLQ* 487; Brudney V 'The Independent Director: Heavenly City or Potemkin Village' (1982) 95 *HarvLRev* 597; Ringe W 'Independent Directors: After the Crisis' (2013) 14 *EBOR* 401 – 424 ; W Ringe 'Beyond "Independent" Directors: A Functional Approach to Board Independence' (2006) 119 (5) *HarvLRev* 1553-1575; Rodrigues U 'The Fetishization of Independence' (2008) 33 *J.Corp.L.* 447. See also the discussion of the independent non-executive director in Chapter 2 below and sources cited.

¹⁶ The now familiar saying ('more law, less justice') is derived from the timeless words of Cicero dating 44 BC (*De Officiis* Book I: 33): Injustice often arises also through chicanery, that is, through an over-subtle and even fraudulent construction of the law. Translation by Walter Miller.

more robust manner. The research further asks whether greater emphasis on the Code is normatively desirable. It does this by considering the practical ramifications of the potential developments on two specific directors' duties that have traditionally been part of common law and is now statute law. It considers this also from a regulatory standpoint, through analysing the doctrines that have informed the regulation of company directors and the perceived aims thereof such as board accountability. The aim in considering these questions is to clarify and deconstruct what has to date been a relatively haphazard approach by the South African judiciary and to respond to misdirected assumptions about the role and relevance of the governance Code under South African law. The aim is further to draw on the conclusions of the research question in order to suggest a more structured and certain approach to the possible integration of the principles of the Code when interpreting and applying Statutory and common law provisions.

This chapter will contextualise the debate and provide an overview of the thesis. Firstly, a broad outline of the history and development of the corporation will highlight the features of the corporate structure that give rise to the various tensions that require regulation. It will then broadly outline the rise of the 'Corporate Governance' agenda and offer a condensed summary of the most notable mechanisms and instruments developed in the wake thereof. This account will consider the developments in general but will specifically offer an introduction to the position in South Africa, with reference to the position in the United Kingdom. The chapter then offers a brief overview of the salient debates and theories that inform the thesis and that will be considered in greater depth and applied to the research question in subsequent chapters. A synopsis of each chapter will follow before final concluding remarks.

2 A Brief Historical Synopsis

a The Limited Liability Company & The Board of Directors

Nobel Prize winner Nicholas Murray Butler famously described the limited liability corporation as ‘the greatest single discovery of modern times ... even steam and electricity would be reduced to comparative impotence without it.’¹⁷ This was hyperbole to be sure,¹⁸ but more than a hundred years after these words were spoken there is still no denying the corporation’s longevity and prevalence.¹⁹

Of course the basic realisation that more can be achieved through combined effort was not a discovery of modern times.²⁰ The Roman law partnership is one example that shows joint ventures were formalised quite early on.²¹ In fact, weak forms of entity shielding could be found as early as the 13th century and representation, limited liability and tradable shares gradually

¹⁷ Extract from a 1911 speech called "Politics and Economics" to the 143rd Annual Banquet of the Chamber of Commerce of the State of New York in 1911 (pp. 43-55) <https://babel.hathitrust.org/cgi/pt?id=coo.31924093105660;view=1up;seq=59> accessed on 25 October 2017. This certainly might be an exaggerated admiration for the private company, but the statement must of course be read in the context of the entire speech to be fair to its author. Tricker echoes the sentiment, calling the modern limited liability model ‘one of the finest systems ever designed.’ Tricker (n5) 6.

¹⁸ As Stern points out: ‘As a legal and political form, the business corporation arose out of various, contradictory, and sometimes disparate, attempts to conceptualize forms of collective action and governance. Thus, as many scholars have shown, its contemporary form is neither inevitable nor necessarily an ideal.’ Philip J. Stern ‘The Corporation in History’ in Grietje Baars and Andre Spicer (eds) *The Corporation: A Critical, Multi-Disciplinary Handbook* (Cambridge UP 2017) 21.

¹⁹ See inter alia: Grietje Baars and Andre Spicer ‘Introduction: Why the Corporation?’ in Grietje Baars and Andre Spicer (eds) *The Corporation: A Critical, Multi-Disciplinary Handbook* (Cambridge UP 2017) 1 – 5.

²⁰ For a comprehensive overview of the history of the company and company law see: Giuseppe Dari-Mattiacci, Oscar Gelderblom, Joost Jonker & Enrico C. Perotti ‘The Emergence of the Corporate Form’ (2017) 33(2) *J Law Econ Organ* 193 for an interesting perspective on the impact of long term capital investment and Asian trade on the development of the corporate form. See also: Susan Watson ‘How the Company Became an Entity: A New Understanding of Corporate Law’ (2015) 1 *J.B.L* 120 where the author considers the development of the modern corporation to shed light on perspectives of agency theory. And see in general: Brian R Cheffins *Corporate Ownership and Control: British Business Transformed* (Oxford UP 2008); WS Holdsworth ‘English Corporation Law in the 16th and 17th Centuries’ (1922) 31(4) *YaleLJ* 382; Rob McQueen *A Social History of Company Law: Great Britain and the Australian Colonies 1854 – 1920* (Ashgate 2009); L E Talbot *Critical Company Law* (Routledge Cavendish 2008), Stern (n18) 21 – 46.

²¹ Dari-Mattiacci and others (n20) 201; Hopt (n5) 1164.

followed suit.²² Medieval jurists in the 14th century began to develop ‘an even more well-articulated theory of the corporation as a transcendent body whose existence amounted to more than simply the sum of its members.’²³ Although medieval guilds and certain political institutions in the late Middle Ages in Western Europe already used a body of representatives, these boards had little other than collective governance in common with their modern counterparts.²⁴

Developments in the 16th and 17th century made it impossible for existing corporate forms and strategies to provide the capital and longevity that more modern commercial endeavours required.²⁵ These challenges could not be resolved without legal intervention, and the modern limited liability company became a necessity,²⁶ such that by the late 1860’s ‘joint stock companies had permeated the Victorian consciousness’.²⁷

The British trading companies (most famously the East India Company) had started life as chartered companies but were later endowed with features similar to those of the seventeenth century joint-stock company.²⁸ As these companies started to trade for their own accounts ‘boards, elected by members, began to manage the affairs of companies and to take business decisions in their best interests, acting as members’ representatives’ and ‘marked the birth of the corporate board as a management organ in the modern sense’.²⁹ At the time the members of the board tended to be heavily

²² Dari-Mattiacci and others (n20) 203; Stern (n18) 22.

²³ Stern (n18) 22.

²⁴ Baum (n15) 7. And see Tricker (n5) 5.

²⁵ Dari-Mattiacci and others (n20) 195; Tricker (n5) 5.

²⁶ Dari-Mattiacci and others (n20) 194. And see in general: WS Holdsworth ‘English Corporation Law in the 16th and 17th Centuries’ (1922) 31(4) *YaleLJ* 382.

²⁷ James Taylor *Creating Capitalism: Joint Stock Enterprise in British Politics and Culture 1800 – 1870* (The Boydell Press 2006) 208. For a chronology of the various statutes promulgated in different jurisdictions at the time see also: Hopt (n5) 1164.

²⁸ Members could no longer trade individually and voting rights were dependent upon each member’s investment in the company’s permanent joint stock. See: Tricker (n5) 5.

²⁹ Baum (n15) 8.

invested in the company and investors elected them on the assumption that they would be acting for the company's benefit in rational self-interest. The board as monitoring instrument was unfamiliar and the more modern divisions between management and the board had not yet developed.³⁰

The corporate form remained a privilege granted by the state on an *ad hoc* basis, and the generally enabling legislation of today only became a common reality during the course of the 18th century.³¹ Processes for registration introduced by the legislation remained cumbersome and restrictive and it is only in 1856 and 1862 with the Joint Stock Companies Act and the Companies Act respectively that one started to see a shift toward a facilitative and enabling regime.³²

In fact, it is the English parliament's reluctance to grant charters for private incorporation following the South Sea Bubble, that led to an enduring distinction between American and English company law traditions.³³ Companies in the United States evolved from the corporation based on a grant from the state, and its laws owe much to rules based on corporate personality.³⁴ This was not the case in England where unincorporated associations or companies were actually no more than large scale partnerships 'legally constructed through an innovative combination of trust law and contract law ... The directors' powers over the unincorporated company's assets were a direct function of the provisions set forth in this deed of settlement.'³⁵ This distinction is significant when considering the

³⁰ Baum (n15) 8.

³¹ Dari-Mattiacci and others (n20) 225.

³² Susan Watson 'How the Company Became an Entity' (n20) 124. The French were in fact the fore runners, creating a form of incorporation, the *Société en commandite par actions* which limited the liability of external investors see: Tricker (n5) 5.

³³ Clarke (n4) 4.

³⁴ Clarke (n4) 5.

³⁵ David Kershaw 'The Path of Corporate Fiduciary Law' (2012) 8 *NYU JLB* 395, 406 where the author gives an overview of these companies, often referred to as "Deed of Settlement Companies". See also: Gower LCB 'Some Contrasts Between British and American Corporation Law' (1956) 69 *HarvLRev* 1371 – 1372.

development and trajectory of the duties that govern company directors, and in turn when considering their reform and interpretation, as later discussions in this thesis will again make apparent.³⁶

At the end of the day, the entity that developed led to significant industrial growth, creating employment and wealth. And although the corporation has undergone a metamorphosis over time, the 'original corporate concept' remains at the heart of contemporary company law.³⁷

Enduring legal mechanisms were gradually devised to regulate this increasingly popular business entity. Most of these rules and regulations centre around certain core attributes of the limited liability corporation or company and it is striking that the rules at the core of corporate regulation are almost identical in most jurisdictions³⁸ (although practical implementation and ancillary rules and regulation result in a corporate law landscape that remains diverse).³⁹ Kraakman pointed out that these universal legal principles speak to structures that could not be replicated by contractual agreement between the parties, but instead required legislative intervention and legal doctrines.⁴⁰

³⁶ See also David Sugarman 'Is company law founded on contract or regulation? The Law Commission's paper on company directors' (1999) 20 *Co Law* 162-183. See also Chapters 6 and 7 where the arguments informing the regulation of corporations are discussed.

³⁷ Tricker (n5) 7.

³⁸ Renier Kraakman and others *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn Oxford 2017) 1.

³⁹ Clarke (n4) 12, where the author considers the "clear divergence between *outsider* systems found in Anglo-American countries with dispersed equity markets, separation of ownership and control and disclosure-based regulation, and the *insider* systems which predominate in Europe, Asia Pacific and other regions of the world, with concentrated ownership, bank finance and the representation of majority interests on the board of directors." And see: Douglas M Branson 'The very uncertain prospect of "global" convergence in corporate governance' (2001) *Cornell Int'l L.J* 321; Thomas Clarke 'The Continuing Diversity of Corporate Governance: Theories of Convergence and Variety' (2016) 16 *Ephemera Theory and Politics in Organization* 19.

⁴⁰ Kraakman and others *The Anatomy of Corporate Law* (n38) 7.

Students of corporate law will be intimately familiar with most of these universal characteristics, such as legal personality and limited liability.⁴¹ However, it is the delegation of management with a board structure that is the characteristic most pertinent to the research that will follow.⁴² In the context of a partnership, all partners usually participate in the day to day management of the business, and certain more fundamental transactions require unanimous consent. It is clearly not possible to manage a company with its constantly changing and often dispersed ownership along these same lines.⁴³ Consequently, management is delegated to a board of directors, reverting to the shareholders only in the case of fundamental decisions. Formally, the board is separate from the company's operational management, and although it is substantially elected by the shareholders it is also distinct from the latter.⁴⁴ In most cases, the board consists of multiple members and this, at least in theory, 'facilitates mutual monitoring and checks idiosyncratic decision-making'.⁴⁵

This almost universal acceptance of the board system is perhaps 'remarkable'.⁴⁶ Prof Harald Baum in a comprehensive paper tracking the rise of the independent director, points out that the company board as we now know it, is a comparatively new development, and one that replaced other successful models.⁴⁷ Its acceptance is arguably even more remarkable given

⁴¹ Kraakman identifies the following common characteristics: (1) legal personality, (2) limited liability, (3) transferable shares, (4) centralized management under a board structure, and (5) shared ownership by contributors of equity capital. See: Kraakman and others *The Anatomy of Corporate Law* (n38) 5.

⁴² As Baum points out, regulation in almost every jurisdiction today "demands or assumes" that a board manages public companies or at the very least that they are managed under the direction of a board. Baum (n15) 7.

⁴³ Kraakman and others *The Anatomy of Corporate Law* (n38) 11.

⁴⁴ Authors point out that it is this structure of delegated authority that leads to the efficiency gains companies are known for. See for example: David Kershaw *Company Law in Context: Text and Materials* (Oxford 2009) 188; Davies and Worthington (n12) 462.

⁴⁵ Kraakman and others *The Anatomy of Corporate Law* (n38) 12.

⁴⁶ Baum (n15) 8.

⁴⁷ Baum (n15) 8. Where the author refers to the example of the pre-Meiji merchant houses of Japan.

that there have been complaints about the ineffectiveness of boards for more or less as long as they have been around. In practice the very concept of the corporate board often turns to caricature as ‘companies with dispersed ownership typically seem to be run in practice by the executive management team or the CEO, and companies with concentrated ownership are often actually run by the dominant shareholder, with the board playing only a peripheral role in both cases.’⁴⁸ In light of this the ubiquitous company board is perhaps not as intuitive a solution to the challenges posed by the corporate form as may at first be assumed. However, despite its perceived shortcomings, the company board (in its various forms)⁴⁹ is a staple of modern commercial life and since the turn of the century international focus has shifted to consider how best to ensure so-called ‘good corporate governance’.⁵⁰

b ‘Corporate Governance’: The rise of a movement

The general history of corporate governance is a vast concept. In fact, even when considering the evolution of the *term* ‘corporate governance’ it is useful to do so with a specific focus in mind. As such, what follows is an overview of the most significant advances emphasizing the increased role of ‘soft law’ mechanisms in the corporate governance arena.⁵¹

⁴⁸ Baum (n15) 7.

⁴⁹ For example, the unitary board popular in the United Kingdom or the two-tier version preferred in Germany. See: Du Plessis JJ ‘Corporate Governance: Some Reflections on the South African Law and the German Two-Tier Board System’ in F Patfield F (ed), *Perspectives on Company Law: 2* (Kluwer Law International 1997) 131.

⁵⁰ See historical overview below at chapter 2 text to notes 44 – 84.

⁵¹ Cheffins B R ‘The History of Corporate Governance’ (2012) ECGI Law Working Paper N°184/2012, 1 <<http://ssrn.com/abstract=1975404>> accessed on 20 August 2017The discussion initially considers developments in the United States as it is in that country that the term ‘corporate governance’ had its genesis before being assimilated worldwide.

There are numerous definitions for the term ‘corporate governance’⁵² but perhaps none as famous as that found in the UK Report of the Committee on the Financial Aspects of Corporate Governance: ‘Corporate Governance is the system by which companies are directed and controlled’.⁵³ It is ‘about the way that power is exercised over corporate entities’⁵⁴ and must be distinguished from management. If management refers to the running of the enterprise, then governance ensures that it is not being run off the road.⁵⁵

These systems for direction and control are generally perceived as essential because of latent agency dilemmas. In the briefest of terms, agency theory revolves around the fact that conflict is inevitable when one person manages the funds of another – or at least this is the conclusion that Adam Smith came to when penning his famous treatise ‘*The Wealth of Nations*’:

Being managers of other people’s money than their own, it cannot be expected that they should watch over it with the same anxious vigilance with which the partners in a private co-partner frequently watch over their own ... Negligence and profusions, therefore, must always prevail more or less in the management of the affairs of a joint stock company.⁵⁶

Nearly two hundred years later, Berle and Means considered the consequences of diffused ownership in what would arguably become the most influential work on corporate governance in the twentieth century,⁵⁷ ‘*The Modern Corporation and Private Property*’.⁵⁸ Although ‘corporate governance’ as a technical term or discipline in its own right, is a recent

⁵² See for example: OECD (2015), G20/OECD Principles of Corporate Governance, OECD Publishing, Paris. <http://dx.doi.org/10.1787/9789264236882-en>

⁵³ Sir Adrian Cadbury *Report of the Committee on the Financial Aspects of Corporate Governance* (1992, Gee & Co Ltd, London) 15.

⁵⁴ Tricker (n5) 4.

⁵⁵ Tricker (n5) 4.

⁵⁶ Adam Smith *An Inquiry into the Nature and Causes of the Wealth of Nations* (Methuen & Co 1776) 264 – 265.

⁵⁷ Clarke (n4) 7.

⁵⁸ Adolf A Berle & Gardiner C Means *The Modern Corporation and Private Property* (1933 The Macmillan Company).

development; it is thus clear that the concept has been a reality since the first conflict arose between investors and management.⁵⁹ In other words: '[c]orporate governance is old, only the phrase is new.'⁶⁰

In fact, the term remained foreign to American industry until the mid-1970's, when the federal Securities and Exchange Commission (S.E.C.) introduced it to the formal agenda.⁶¹ Although corporations had been growing and flourishing in the United States following World War II, increased numbers, sizes and revenue did not coincide with any real sophistication in the management of corporate entities.⁶² Widespread corporate bribery and managerial misconduct during the late 1970's led the SEC to eventually convince the New York Stock Exchange in 1976 to require listed companies to appoint audit committees comprised of non-executive directors and this was made part of the listing requirements.⁶³ This coincided with increased debate about the duties of boards of directors toward other stakeholders in both America and in Europe, and the promotion of two-tiered boards on the continent.⁶⁴

'Corporate governance' had become irrevocably part of the conversation, and from several corners concerns were being voiced about the poor state of governance in large American companies. Primarily, these concerns centred around the complete lack of oversight on the part of the board, allowing management to make ill-informed and self-serving decisions with relative impunity.⁶⁵ There were several calls to 'return the board to its historical role as internal auditor of the corporation responsible for

⁵⁹ Cheffins 'The History of Corporate Governance' (n51) 1; Clarke (n4) 1, 7.

⁶⁰ Tricker (n5) 4.

⁶¹ It did so, by increasingly considering the accountability of corporate managers as part of its regulatory remit. Cheffins 'The History of Corporate Governance' (n51) 2.

⁶² Cheffins 'The History of Corporate Governance' (n51) 1.

⁶³ Cheffins 'The History of Corporate Governance' (n51) 3; Berle & Means *The Modern Corporation and Private Property* (1933) 9.

⁶⁴ Tricker (n5) 9.

⁶⁵ Cheffins 'The History of Corporate Governance' (n51) 5.

constraining management from violations of law and breaches of trust'⁶⁶ and the debate was picked up in the United Kingdom.⁶⁷ However, the election of Ronald Reagan in 1980, and a shift in political sensibilities, effectively stopped the enthusiastic reforms of the 1970's in their tracks.⁶⁸

The corporate governance agenda regained lost momentum during the 1980's. A wave of hostile takeover bids, and concomitant managerial defence strategies caused the pendulum to swing in a shareholder-centric direction and a 'shareholder oriented corporate governance infrastructure ... emerged'.⁶⁹ The late 1980's and early 1990's remain significant in shifting the focus of the governance debate towards shareholders and shareholder returns.⁷⁰

Corporate Governance Codes arrived in the 1990's, pioneered by the United Kingdom's Cadbury Report in 1992.⁷¹ Others soon followed, including the Vienot Report (1995, France), the King Report (1995, South Africa), and the Toronto Stock Exchange Recommendations on Canadian Board Practices (1995, Canada).⁷² As a rule, the Codes tended to be concerned with the potential for abuse of corporate power. By the end of the 20th century there seemed to be a working governance system in place, but it proved to be the calm before the storm as an incredible spate of corporate collapses in America and around the world wreaked havoc during the early 2000's.⁷³ In

⁶⁶ Cheffins 'The History of Corporate Governance' (n51) 5.

⁶⁷ Tricker (n5) 10.

⁶⁸ Law and economics scholars also shunned the governance agenda, contending that the debate had failed to take key points into consideration, such as the impact of market forces on executive behaviour. Cheffins 'The History of Corporate Governance' (n51) 8.

⁶⁹ Cheffins 'The History of Corporate Governance' (n51) 11 - 12.

⁷⁰ Cheffins 'The History of Corporate Governance' (n51) 15. See also an overview of the development of law and economics scholarship discussed in Chapter 6, text to note 66 – 67 where the impact of the 1980's takeover driven corporate culture is considered further.

⁷¹ Tricker (n5) 12.

⁷² Tricker (n5) 13.

⁷³ There are many famous examples, but perhaps none more than the collapse of Enron in the United States. See n 3 above.

America it prompted the Sarbanes-Oxley Act (SOX) to be rushed through in 2002, while other jurisdictions fervently redrafted or updated existing Governance Codes.⁷⁴

The Organisation for Economic Co-operation and Development (OECD) gained prominence at an international level, publishing its Principles of Corporate Governance in 1999.⁷⁵ The principles finally adopted by the OECD were informed entirely by recommendations made by the Business Sector Advisory Group on Corporate Governance, set up by OECD Ministers in 1996 and mirror those contained in the United Kingdom's corporate governance code at the time almost exactly. As Dignam points out, this illustrates the 'Anglo-Saxon orientation' of the principles, the consequences of which are manifold.⁷⁶ A number of initiatives in the EU followed, most notably the European Commission's decision to set up a Group of High-Level Company Law Experts to consider the modernisation of company law in Europe.⁷⁷

As mentioned, almost all advanced and developing countries have by now introduced Corporate Governance Codes of best practice and many have enacted new company legislation.⁷⁸ The corporate governance advisory profession has 'grown in direct correlation with corporate boards' ever-increasing governance responsibilities and is now recognised as a distinct City sub-industry alongside traditional sectors such as commercial law and

⁷⁴ Tricker (n5) 17.

⁷⁵ Dignam A 'Exporting corporate governance: U.K. regulatory systems in a global economy' (2000) 21(3) *Co Law* 70, 74.

⁷⁶ Dignam A 'Exporting corporate governance' (n75) 74. The author considers the typically Anglo-Saxon approach of 'negotiated regulation' that the OECD concomitantly embraces and points to the shortcomings of this regime. His views are considered in greater detail in Chapter 7, see text to n 30.

⁷⁷ See European Commission website at: https://ec.europa.eu/info/business-economy-euro/doing-business-eu/company-law-and-corporate-governance_en. For an overview of the development of European Company Law and governance see: Hopt (n5) 1174; Copp (n3) 66.

⁷⁸ Tricker (n5) 3; Hopt (n5) 1182. Hopt points out that the various reasons are given for adopting governance codes in different jurisdictions, among them simply imitation of even 'legal fashion'.

investment banking.’⁷⁹ Despite this, there remains ‘considerable uncertainty’⁸⁰ about the definition and exact role of corporate governance, with Tricker referring to it as ‘a subject in search of its paradigm’.⁸¹

In searching for this paradigm, Wymeersch notes that ‘[C]orporate [G]overnance [C]odes function within a given legal environment. The interaction with the legal system is a complex matter that differs considerably from state to state ... Enforcement techniques and efficiency will be directly dependent on the legal nature of the codes’.⁸² This is one of the core concerns of the research undertaken below – the efficacy of the interaction between the Corporate Governance Code and the formal legal order as facilitated by the courts. As such, the discussion will proceed to consider (in overview) the South African legal environment within which its governance codes must function.

3 An overview of the Legal Landscape

a South Africa

A review of company law taking up almost the entire first decade of the 21st century, culminated in a new piece of legislation to govern South African corporate entities: the Companies Act 71 of 2008.⁸³ The Act made sweeping changes, and broke ranks with English law in several respects, choosing instead to borrow concepts from jurisdictions such as Australia, and the United States.⁸⁴ The new legislation embraced a facilitative approach, with

⁷⁹ Mark T Moore *Corporate Governance in the Shadow of the State* (Hart 2013) 12.

⁸⁰ Moore *Governance in the Shadow* (n79) 12.

⁸¹ Tricker (n5) 74.

⁸² E Wymeersch ‘The Enforcement of Corporate Governance Codes’ (2006) 6 *J. Corp. Law Stud.* 114.

⁸³ Farouk HI Cassim and others (eds) *Contemporary Company Law* (2nd edn, Juta, 2012) 2.

⁸⁴ Cassim and others *Contemporary Company Law* (n83) 2. Despite this, many similarities between South African and English company law remain. For a further

certain core mandatory provisions being supplemented by ‘opt-in/opt-out’ provisions that companies can choose to incorporate when drafting and refining the company constitution – referred to as the Memorandum of Incorporation.⁸⁵ To achieve this, the Act distinguishes between so-called ‘alterable provisions’⁸⁶ and ‘unalterable provisions’,⁸⁷ with the latter essentially comprising the mandatory rules that companies cannot opt out of.⁸⁸

Like its English counterpart the legislation does not differentiate between executive and non-executive directors, nor does it reference the so-called ‘independent non-executive’ director.⁸⁹

The drafters’ decision to partially codify directors’ duties generated extensive debate.⁹⁰ The arguments echo those raised when the Law Commission and Company Law Review in the United Kingdom proposed a

discussion of the impact of English company law on South African corporate law jurisprudence and its continued importance see text to n 116 – n 126.

⁸⁵ The approach is not unique to South Africa and is especially reminiscent of corporate law in the United States and Delaware in particular. See Kraakman and others *The Anatomy of Corporate Law* (n38) 19 – 20.

⁸⁶ Defined in section 1 of the Act as “a provision of this Act in which it is expressly contemplated that its effect on a particular company may be negated, restricted, limited, qualified, extended or otherwise altered in substance or effect by that company’s Memorandum of Incorporation.”

⁸⁷ Defined in section 1 of the Act as “a provision of this Act that does not expressly contemplate that its effect on any particular company may be negated, restricted, limited, qualified, extended or otherwise altered in substance or effect by a company’s Memorandum of Incorporation or rules.”

⁸⁸ An in-depth discussion of the application of these provisions and their interaction with existing company documentation etc falls outside of the scope of this thesis. See however: Helena H Stoop ‘Alterable and unalterable provisions of the Companies Act 71 of 2008: Recent Cases Expose Inherent Uncertainties’ *JCCLP* Volume 1 (2016) 40.

⁸⁹ The definition of ‘director’ in section one is broad enough to include these as well as so-called ‘shadow directors’. For a discussion of the definition see Kathy Idensohn ‘The Regulation of Shadow Directors’ (2010) 22(3) *SA Merc LJ* 326 – 345. See further chapter 2 at n 27.

⁹⁰ Natasha Bouwman ‘An appraisal of the modification of the director’s duty of care and skill’ (2009) *SA Merc LJ* 509; Irene-Marie Esser ‘Codification of directors’ duties’ (2004) *Juta’s Bus Law* 26; McLennan JS ‘Directors’ fiduciary duties and the 2008 Companies Bill’ (2009) *TSAR* 184.

‘high level statutory statement’ of directors’ duties.⁹¹ Proponents hoped that codification could clarify and consolidate what was traditionally an area of law that even legal practitioners navigated with some difficulty – let alone lay persons acting as company directors.⁹² On the other hand, critics argued that codification and any rigid bright lines could ‘freeze’ the law, and impede further development in response to changing circumstance.⁹³ Davies and Worthington explain that these concerns could be refuted on two fronts. First, the statutory statement of duties was always intended as a ‘high level’ statement, and it gives the courts ‘enough interpretative scope when applying the principles to the changing circumstances of commercial life’. Furthermore, section 170(4) presupposes that the statutory duties ‘shall be interpreted and applied in the same way as the common law duties or equitable principles’ and also that ‘regard shall be had to the corresponding common law rules and equitable principles in interpreting and applying the general principles.’⁹⁴

The effect of the first statement is clearly that existing case law on the common law duties remain relevant when interpreting the new statutory duties.⁹⁵ The impact of the second statement is not as immediately apparent, but according to Davies and Worthington its effect would be to allow the courts to continue to consider developments in equivalent common law

⁹¹ *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties*, Law Com. No. 261 and Scottish Law Com. No. 173, Cm. 4436 (1999); CLR, Final Report, Ch.3 and Annex C.

⁹² Although as Davies and Worthington point out, ‘the behavioural premises upon which this view was based were never extensively investigated.’ Davies and Worthington (n12) 463.

⁹³ Davies and Worthington (n12) 463.

⁹⁴ Davies and Worthington (n12) 464.

⁹⁵ As Keay points out: ‘The rules and principles that have been replaced by the statement of general duties will not apply directly, but it is highly likely that the approaches and views of the courts in defining directors’ duties over many years will be very influential in the manner in which the courts decide to interpret the new statutory provisions. So, in cases where the statute adopts wording and terminology that is similar to the pronouncements of common law rules and equitable principles, case law is likely to be followed faithfully.’ Andrew Keay *Directors’ Duties* (Jordan 2009) 59.

duties that apply to trustees and agents as they have traditionally done when constructing directors' duties.⁹⁶

Any confusion regarding the relationship between the common law and statutory duties is dealt with by these sections read with section 170(3) which states that the general duties contained in the statute have effect in place of the common law. However, this does not mean that all difficulties are eliminated. Many of the statutory statements comprise of more than a mere restatement of the common law. In instances where the statute departs from the common law, reference to the latter is naturally no longer appropriate. The Act does not indicate at face value where it deviates from the common law however, and as any inquiry must start by determining where the act confirms the common law and where it departs from it.⁹⁷

In the South African context, it remains unclear whether the status quo aligns with this position in the UK following the 2006 Companies Act.⁹⁸ It is namely also possible that it could simulate Australian law, where a director owes his company statutory duties, but codification did not displace his common law duties which apply in tandem.⁹⁹ The favoured approach following the promulgation of the 2008 Companies Act has been that the common-law duties remain intact and can serve as a basis for a separate cause of action, alongside the codified duties.¹⁰⁰ The common law applies unless expressly excluded or in conflict with a statutory provision. Although

⁹⁶ Davies and Worthington (n12) 464.

⁹⁷ Davies and Worthington (n12) 464. And see: Keay *Directors' Duties* (n95) 59.

⁹⁸ On the position in the UK see further: Keay *Directors' Duties* (n95) 174. Section 170(3) of the 2006 Act states that not all duties are set out in the 2006 Companies Act and the courts would therefore remain free to develop these aspects of the law. Davies and Worthington name as an example the duties of directors toward company creditors. See: Davies and Worthington (n12) 464.

⁹⁹ Keay *Directors' Duties* (n95) 174.

¹⁰⁰ See for example: *Mthimunye-Bakoro v Petroleum Oil And Gas Corporation of South Africa (SOC) Limited and Another* 2015 (6) SA 338 (WCC) where Davis J remarked that: ". . . recourse may [still] be had to the common law which, save for the express legislative exclusions remains the structure of company law upon which the superstructure of the Act rests." See also: *Henochsberg on the Companies Act 71 of 2008* (Issue 18 2018) 290(5); Bouwman (n90) 516.

the duties are codified, their contents are not defined – this is left to the common law and it is in fact in this manner that one is able to achieve the flexibility that such a scheme requires, although, as Delpont points out, at the cost of the very legal certainty that it sought to achieve.¹⁰¹ The approach also accords with the presumption, in statutory interpretation, that the legislature does not seek to change the existing law unless expressly stated.¹⁰²

In addition to the 2008 Companies Act, South African regulators have chosen to embrace a scheme similar to that in the United Kingdom, in the form of a voluntary Code of Governance principles. In fact, as mentioned above,¹⁰³ by the time Enron and company were making headlines, South African companies had already grown accustomed to the requirements of the King Code of Corporate Governance. The King Committee had been formed in 1992, under the auspices of the Institute of Directors of Southern Africa and their report, and a code of best practice (known as the King Code of Corporate Governance) was published in 1994.¹⁰⁴

¹⁰¹ *Henocheberg on the Companies Act 71 of 2008* (Issue 18 2018) 287.

¹⁰² See for example: *Casserley v Stubbs* 1916 TPD 310 at 312 where Wessels J sets out the position as follows: ‘It is a well-known canon of construction that we cannot infer that a statute intends to alter the common law. The statute must either explicitly say that it is the intention of the legislature to alter the common law, or the inference from the ordinance must be such that we can come to no other conclusion than that the legislature did have such an intention.’ See also: *Dhanabakium v Subramanian* 1943 AD 160; *Rand Bank Bpk v Regering van die RSA* 1974 4 SA 764 (T) 767; *Bills of Costs (Pty) Ltd v The Registrar, Cape* 1979 3 SA 925 (A) 942; *Kaplan v Inc Law Society Tvl* 1981 2 SA 762 (T) 770; *Law Society of the Cape of Good Hope v C* 1986 1 SA 616 (A) 639E; *Skyway Management Ltd v Telkom SA Bpk* 2001 2 SA 779 (T) 784. And see: LM Du Plessis *Statute Law and Interpretation* in 25(1) *Lawsa* (reissue, 2001) para 340.

¹⁰³ See text to note 73 above.

¹⁰⁴ On the history and development of the South African corporate governance code in general see: Esser I & Delpont P ‘The South African King IV Report on Corporate Governance: is the crown shiny enough?’ (2018) 39(11) *Co Law* 378; JJ Du Plessis ‘Corporate Governance: Some Reflections on the South African Law and the German Two-Tier Board System’ in F Patfield F (ed), *Perspectives on Company Law: 2* (Kluwer Law International 1997) 131.

Despite the fact that it was ground-breaking at the time, King I dealt mainly with financial and regulatory aspects of corporate governance and it was soon clear that an updated version would be required. The King committee thus developed a second iteration of the Report which also contained a Code of Corporate Practices and Conduct. King II confirmed a move away from the single bottom line to embrace a so-called ‘triple bottom line’ approach – the latter taking account of the company’s social, environmental and economic impact.¹⁰⁵

The financial crisis of 2007/2008 (which happened to coincide with the promulgation of South Africa’s 2007 Companies Act) prompted yet another revision of the Code. King III came into effect on 1 March 2010. It remained a ‘non-legislative code on principles and practices’, but although it was written in accordance to the *comply or explain* principle commonly used, it specifically introduced a so-called ‘*apply or explain*’ regime to governance.¹⁰⁶ King III also refined the triple bottom line concept, choosing instead to use the term ‘triple context’ to reflect the interconnectivity of these different dimensions; the economy, society, and the natural environment. It was this development that prompted the novel approach of integrated reporting which was favourably received elsewhere.¹⁰⁷

A further revision was announced in 2014 and a process of research and consultation resulted in the publication of the most recent King Report and Code, King IV, in 2016. It replaced King III in its entirety, and although it covered the same material it had taken account of subsequent international developments and had a simpler and arguably more accessible structure.¹⁰⁸

¹⁰⁵ Esser I & Delport P (n104) 378. And see: Cassim and others *Contemporary Company Law* (n83) 437, Philip Armstrong, ‘The King Report on Corporate Governance’ (1995) 3 *Juta’s Business Law* 65.

¹⁰⁶ Esser & Delport (n104) 378.

¹⁰⁷ Esser I & Delport P (n104) 378. And see: Cassim and others *Contemporary Company Law* (n83) 437.

¹⁰⁸ Esser I & Delport P (n104) 378. See also:

In the case of most jurisdictions with self-regulatory Codes in place, the Code applies to listed entities only, and is usually enforceable indirectly as part of a set of listing requirements set out by a relevant exchange. This was also the case in South Africa, with the first two iterations of the King Code finding application mainly in the case of listed entities, government institutions and banks,¹⁰⁹ and being ‘enforced’ indirectly as part of the Johannesburg Stock Exchange’s Listing Requirements.¹¹⁰ However, the drafters of the third updated version of the code, King III¹¹¹ were ambitious enough to declare that it ‘applies to all entities regardless of the manner and form of incorporation or establishment and whether in the public, private sectors or non-profit sectors’ stating that they had ‘drafted the principles so that every entity can apply them and, in doing so, achieve good governance’.¹¹² King IV is ‘soft law’. The only direct reference to it that can be found in South Africa’s Companies Act is that in regulation 54, which determines that a prospectus must include a narrative statement setting out how the company has applied the principles of the King Report and Code¹¹³ and any reasons for a failure to apply them.¹¹⁴

The King committee have continued to grapple with issues surrounding the appropriate application and enforcement of the Codes. South African courts have also increasingly been making statements in *obiter* that may imply an

¹⁰⁹ The Code also applied to Banks, financial and insurance entities as defined in the various legislation regulating the South African financial services sector, public sector enterprises and agencies, including any department of State or administration in the national, provincial or local sphere of government. All other companies were encouraged to comply with the Code to the extent applicable. King Committee on Corporate Governance *Report on Corporate Governance for South Africa* (Institute of Directors in Southern Africa, 2002) 21.

¹¹⁰ Esser & Delpont (n104) 378.

¹¹¹ King Committee on Corporate Governance *Report on Corporate Governance for South Africa* (Institute of Directors in Southern Africa, 2009).

¹¹² King Committee on Corporate Governance *Report on Corporate Governance for South Africa* (Institute of Directors in Southern Africa, 2009) 17.

¹¹³ This is in turn defined by regulation 47(a) as ‘the King Report on Governance for South Africa and the King Report and Code of Governance Principles (King III), as amended or replaced from time to time’.

¹¹⁴ See also: Esser & Delpont (n104) 384.

indirect application of the codes in proceedings seeking to hold company directors personally liable for breaches of their statutory and common law duties.¹¹⁵ Such references to the King Code in the cases decided to date have been cursory and the courts do not give any clear indication of the extent of the interaction between the statutory and common law provisions and the governance code.¹¹⁶ The most recent draft of the Code refers expressly to these decisions and developments in emphasizing its importance and application outside the traditional sphere of the listed company.¹¹⁷ The code also contains so-called ‘sectoral supplements’, that are clearly not aimed at listed companies.¹¹⁸

It seems beyond doubt that the drafters of at least the latest two versions of the King Code seemed to have in mind the broadest possible application of its principles. Although it is too soon to draw any definitive conclusions from the case law to date, the South African courts at least to some extent, agree, even edging in the direction of formally reading the principles of the code into black letter law. These developments in South Africa raise interesting questions and depending on how the legislature and the courts choose to proceed, may have a far-reaching impact on the landscape of corporate law and the legal principles governing the conduct of company directors.

b The Jurisdictions Chosen for Comparative Analysis

¹¹⁵ See for example: *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* (2006) 5 SA 333 (W), *Levenstein v S* [2013] 4 All SA 528 (SCA); *Kalahari Resources (pty) Ltd v Arcelormittal SA and others* [2012] 3 All SA 555 (GSJ); *Council for Medical Schemes and Another v Selfmed Medical Scheme and Another* [2011] ZASCA 207; *South African Broadcasting Corporation Ltd and another v Mpofu* [2009] 4 All SA 169 (GSJ).

¹¹⁶ See 1.5 below.

¹¹⁷ King Committee on Corporate Governance *Report on Corporate Governance for South Africa* (Institute of Directors in Southern Africa, 2016) 17.

¹¹⁸ King Committee on Corporate Governance *Report on Corporate Governance for South Africa* (Institute of Directors in Southern Africa, 2016) 74 – 117.

Although Roman-Dutch law forms the dominant basis for South Africa's common law, the 'original' Roman-Dutch law has been extensively influenced by English Law, and 'what today is known as 'South African law' can perhaps best be described as a hybrid consisting of Roman-Dutch and English law elements adapted to peculiarly South African circumstances and needs.'¹¹⁹ It is also the case that many South African statutes, among them in areas such as shipping, company law, insurance law, and the laws of arbitration, negotiable instruments, and evidence are identical to United Kingdom enactments or import English law 'in various decisive respects'.¹²⁰ This presents difficulties as far as the interpretation of these statutes are concerned. The courts are allowed readily to revert to Roman-Dutch law as 'basic common law' but English law does not have similar default authority.¹²¹

A summary of the approach favoured approach is that South African courts treat the decisions of British or other Commonwealth courts as having 'considerable persuasive force' although these decisions are not binding.¹²² Furthermore, as Colman J pointed out in *Montelindo Compania Naviera SA v Bank of Lisbon & SA Ltd*¹²³ it is not necessarily or invariably sound to assume that a word appearing in the English text of a South African statute would bear the same meaning in South Africa as it would in England, as 'a word may acquire a meaning different from the one which it bears in

¹¹⁹ Du Plessis (n102) par 372.

¹²⁰ Certain sections are incorporated verbatim while in other cases the content of a section is incorporated using different words. Du Plessis (n102) par 372.

¹²¹ Du Plessis (n102) par 372. Although the courts seemed readily to revert to English law, see for example: *R v Myburgh* 1916 CPD 676 680; *Beukes v Knights Deep Ltd* 1917 TPD 683 689; *Osaka Mercantile Steamship Co Ltd v SAR&H* 1938 AD 146 174.

¹²² Du Plessis (n102) par 372. However, this is subject to the caveat that such a reliance on foreign law may not conflict with any existing Roman Dutch common law or import foreign principles into South African law. See *Roodepoort United Main Reef GM Co Ltd (in liquidation) v Du Toit* supra 71–72. See also *In re Trans-African Insurance Co Ltd (in liquidation)* 1958 3 All SA 265 (W); 1958 4 SA 324 (W) 328A–C; *S v Mokoena* 1967 1 All SA 572 (A); 1967 1 SA 440 (A) 445A.

¹²³ 1969 1 All SA 241 (W); 1969 2 SA 127 (W) 131F.

England'¹²⁴ under South African usage. Different contexts also have to be born in mind. Although it has been suggested that one can assume that the South African legislature was aware of the judicial interpretations placed upon English legislation when taking over those statutes or provisions contained in them (in particular where the wording is identical), Du Plessis points out that this assumption cannot invariably hold sway. He emphasises that 'much will depend on the nature and history of the enactment in question and the bearing which South African common law or statute law has on the subject matter of the enactment.'¹²⁵ There is no doubt that English law has had a significant impact on South African company law. The concept of the limited liability company spread throughout the 19th century British Empire, and the company laws of South Africa and other Commonwealth Countries still reflect these origins.¹²⁶ In fact, Du Plessis made the following telling observation on the nature of South African company law in 1997:¹²⁷

Factors like the influence of European company law on the United Kingdom, a relatively long period of isolation from international influence on South African company law and a conservative approach as far as a comprehensive overview of South African corporate law is concerned, resulted in an ironical situation, namely that South Africa has at the moment probably a more traditional British company law system than the Brits themselves.

What is more, it is particularly on the law that governs directors' duties that English law has had a significant impact and the courts have referred liberally

¹²⁴ 1969 1 All SA 241 (W); 1969 2 SA 127 (W) 131F.

¹²⁵ Du Plessis (n102) par 372.

¹²⁶ Stephen D Girvin 'The Antecedents of South African Company Law' (1992) 13(1) *J.Leg.Hist.* 63; Tricker (n5) 7.

¹²⁷ Du Plessis 'South African Law and the German Two-Tier Board System' (n104) 135.

to English precedent in developing both the duty of care and skill and several fiduciary duties in South African Law.¹²⁸

However, there are other reasons why it is useful to consider English law when analysing this particular research question. As mentioned, the United Kingdom has also opted for a regulatory regime based partially on a voluntary code of best practice. The original Cadbury Code strongly influenced the drafters of South Africa's first corporate governance code,¹²⁹ and the drafters have continued to take note of developments in the United Kingdom when updating the Code and Report.¹³⁰

Apart from the United Kingdom, the thesis will refer to American literature and to a limited extent American case law. These sources are pertinent to various issues touched upon by the research. Most importantly, the so-called 'Law and Economics' movement developed predominantly in the United States.¹³¹ The theories and philosophies developed by law and economics scholars have had a significant impact on perceptions of the role of company law and the appropriate regulation of corporate entities.¹³² Paragraph 4 below gives a brief overview of these debates and they are engaged more fully in Chapter 6 of the thesis. It is also interesting and at times helpful to consider American law as a juxtaposition to South African and English law. This is due to the fact that the United States, through the

¹²⁸ *Fisheries Development Corporation of SA Ltd v Jorgensen and Another* 1980 (4) SA 156 (W) 165 where Margo J concluded that the 'essential principles' of this branch of South African company law are the same as those in English law and as such, 'the English cases provide a valuable guide.' See also: *Du Plessis NO v Oosthuizen* 1999 (2) SA 191 (O) 201. And see chapters 3 and 4 and the cases cited.

¹²⁹ See above text to notes 71 – 77.

¹³⁰ Brian Cheffins 'Corporate Governance Reform: Britain as an Exporter' David Hume Institute in *Corporate Governance and the Reform of Company Law*, Hume Papers on Public Policy: Volume 8 No. 1 (Edinburgh University Press, 2000) 7. On the widespread appropriation of the Cadbury report and some criticisms of this see also: Dignam A 'Exporting corporate governance' (n75).

¹³¹ See Chapter 7.

¹³² See in overview on the role of the law and economics movement and prominent scholars: Hopt (n5) 1184.

promulgation of the Sarbanes-Oxley Act (SOX) ¹³³ have opted for a mandatory regime to regulate corporate governance. Finally, the South African legislature in drafting the 2008 Companies Act, opted to import several distinctly ‘American’ features, and some of these are germane to the issues at hand.¹³⁴

Amongst other things, the research will turn to the enforcement of directors’ duties and the impact that failed enforcement might have on accountability in general. In this context, brief reference will be made to the position in Australia where the public enforcement of directors’ duties have apparently resulted in a more robust regime.¹³⁵ However, the debate surrounding the public enforcement of directors’ duties is only ancillary to the central research questions addressed in this thesis and as such Australian law and scholarship will not be dealt with in as much depth as other jurisdictions.

4 Theories and Debates that Inform the Thesis

Having considered common features of company law across a number of jurisdictions, Armour, Hansman and Kraakman identify two general and primary functions thereof. The first is to create an appropriate structure and to then buttress this structure with rules to regulate internal affairs, and the second is to control conflicts of interest between various stakeholders or corporate communities.¹³⁶ It is these conflicts, that economists have termed

¹³³ Tricker (n5) 17.

¹³⁴ Most notable examples are found in the following sections of the 2008 Act: Section 164 which incorporates a version of the American ‘appraisal remedy’; section 76 which ostensibly incorporates a version of the American ‘business judgement rule’; and section 165 which incorporates elements of the American derivative action in the form of a demand procedure. For further analysis pertaining to section 76 and section 165 see chapters 5 and 7 respectively.

¹³⁵ See Chapter 7, text to note

¹³⁶ Kraakman and others *The Anatomy of Corporate Law* (n38) 28.

the ‘agency dilemmas’ or ‘principal-agent’ problems.¹³⁷ Armour, Hansman and Kraakman summarise the phenomenon as follows:¹³⁸

...an “agency problem” – in the most general sense of the term – arises whenever one party, termed the “principal,” relies upon actions taken by another party, termed the “agent,” which will affect the principal’s welfare. The problem lies in motivating the agent to act in the principal’s interest rather than simply in the agent’s own interest...

The authors point out that almost any contractual relationship in terms of which one party promises performance to another may potentially be subject to an agency problem, not least because there is usually some extent of asymmetry of information. The principal is often unable to verify whether the agent’s performance is what was agreed upon, which in turn might incentivise the agent to act opportunistically.¹³⁹

This approach - which sees the corporation through the lens of the agency dilemma - is related to a school of thought known as the ‘nexus of contracts’ theory or contractarianism in short.¹⁴⁰ Contractarian scholars see the company as a series of contracts, giving rise to the agency dilemmas outlined above. As Kershaw explains, these contracts pertain not only to suppliers of labour and other resources, but also to suppliers of equity capital – the

¹³⁷ See M.C.Jensen and W.H. Meckling, ‘Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure’ (1976) *JFE* 305. A wealth of literature explores, analyses and discusses agency theory in a great deal of depth. Further sources will be considered in greater detail in Chapter 6, text to notes 84 – 102. See for example: Kraakman and others *The Anatomy of Corporate Law* (n38) 28. And see for an overview of the corporate agency problem: Kershaw *Company Law in Context* (n44) 163 – 177. See also Watson ‘How the Company Became an Entity’ (n20) 120.

¹³⁸ Kraakman and others *The Anatomy of Corporate Law* (n38) 29.

¹³⁹ Kershaw in this regard distinguishes between direct and indirect transfer of value (or agency costs). Self-dealing, senior management remuneration and business opportunities are examples of the former, while shirking and incompetence and perquisites are examples of the latter. Kershaw *Company Law in Context* (n44) 85.

¹⁴⁰ D Attenborough, ‘Empirical insights into corporate contractarian theory’ (2017) 37 (2) *Legal studies* 191, 206; Kershaw *Company Law in Context: Text and Materials* (Oxford 2009) 85.

shareholders. The terms of the contract are found in company law and the company constitution and even in the largest of companies, scholars contend, there is some form of bargaining to be found.¹⁴¹ Although this does not take the form of traditional contractual negotiations, there is an implicit bargaining process in place which operates via the market. The argument is that sophisticated shareholders will evaluate the rules of governance offered by a company in its constitution. Management will be pressured into offering shareholders 'constitutional terms that maximize what equity investors will pay for the shares. Where companies do not offer such terms those sophisticated shareholders will pay less for the shares. According to contractarians, therefore, the corporate constitution represents part of (together with company law) the corporate contract, and an implicitly negotiated corporate contract.'¹⁴²

Contractarianism became the dominant ideology by the end of the 20th century and is often used to justify an approach to corporate governance that emphasises shareholder rights or profit maximisation. The influence that this theory has had on corporate law scholars, the courts and regulators alike is particularly significant when unpacking the issues related to the research question.¹⁴³

This is because the issues that it raises speak to the very core of how one chooses to view the role of corporate law. Contractarians favour the view that companies should be regulated with a 'private law' slant and that the parties should be left to determine how they want to structure their relationships with minimum regulatory interference. Where laws and regulations are put in place, these should serve mainly to facilitate the formation of this contractual nexus and to eliminate transactions costs associated with having to negotiate and bargain to achieve optimal

¹⁴¹ Kershaw *Company Law in Context* (n44) 85.

¹⁴² Kershaw *Company Law in Context* (n44) 85.

¹⁴³ Simon Deakin 'The Corporation as Commons: Rethinking Property Rights, Governance and Sustainability in the Business Enterprise' (2012) 37 *Queen's L.J.* 341

contractual outcomes for the parties involved.¹⁴⁴ This view would see the role of corporate law as reflecting or stating the norms and practices that already exist and rules that have developed endogenously over time. A different point of view sees corporate law from a ‘public’ perspective and acknowledges its role as ‘norm setting’.¹⁴⁵ The debate is nuanced and comprehensive, but the thesis will attempt to engage with it to the extent necessary to adequately unpack the normative issues underlying the research question.

This is one prism through which to view a multi-faceted debate. Regulation does not exist in a vacuum, and as Bebchuk and Roe posit in their theory of path dependence, historical facts such as ownership structures certainly impact the development of corporate entities (and by extension their regulation) at later stages.¹⁴⁶ The fact that globalisation has not resulted in a more comprehensive convergence of corporate law further illustrates the impact of culture, socio-economic circumstances and political ideology in the formulation of corporate law and policy and attitudes towards regulation.¹⁴⁷ It is simply not possible to engage with all of these matters to the extent that would do them justice in a single thesis. As such, the analysis that will follow in subsequent chapters opts to consider only the most dominant theories that have directly informed the corporate governance debate and are most strongly related to the research question.

5 Chapter Overview

¹⁴⁴ Moore *Governance in the Shadow* (n79) 2.

¹⁴⁵ Moore *Governance in the Shadow* (n79) 2.

¹⁴⁶ Lucian Arye Bebchuk and Mark J. Roe ‘A Theory of Path Dependence in Corporate Ownership and Governance’ (1999) 52(172) *Stan.L.Rev* 127.

¹⁴⁷ Du Plessis JJ and Others *Principles of Contemporary Corporate Governance* (4th edn Cambridge UP 2018) 19. See also: Douglas M Branson ‘The very uncertain prospect of “global” convergence in corporate governance’ (2001) *Cornell Int’l L.J* 321; Clarke ‘The Continuing Diversity of Corporate Governance’ (n39) 19.

Before turning to the contents and application of the directors' duties central to the research chapter 2 will consider the individuals that these rules pertain to. For reasons set out below, the thesis will consider much of the debate through the prism of the independent non-executive director.¹⁴⁸ Chapter 2 will therefore define what is meant by the term 'independent non-executive director' and analyses the role and position of the independent non-executive director generally, with emphasis on the regulatory framework in South Africa. It also considers the importance of the independent non-executive director in the broader context of the governance regime and overviews weaknesses of the office identified in South Africa and elsewhere especially following the financial crisis.

Having considered the role of the independent non-executive director the analysis will turn to the duties themselves. The research homes in on the two duties that, in conjunction, have been described as an expression of 'the law's view on how directors should discharge their functions on a day-to-day basis.'¹⁴⁹ Chapters 3 and 4 will consider the duty of care and skill and the duty to act in the best interests of the company in some detail. The aim of this line of analysis is to consider whether these duties are viable candidates for such treatment in the first place. It is only by considering the origins of the duties, how they have been developed by the courts to date and where the judiciary and academic opinion currently stand on their role and application that one can safely make any predictions or recommendations regarding their potential future development. It is exactly this task which chapter 3 undertakes in relation to the duty of care and skill. Following this, chapter 4 will turn to the duty to act in the best interests of the company with similar aims.

The duty of care, skill and diligence is perhaps the most apparent choice in considering any role that the governance codes might play in the

¹⁴⁸ Demetra Arsalidou 'The liability of non-executive directors for negligent omissions: a new approach under legislation?' (2002) 23(4) *Co Law* 107,107.

¹⁴⁹ Davies and Worthington (n12) 501.

development and interpretation of this new legal regime. The duty and the debates that have surrounded it speak to perceptions regarding the role of the company director and the extent to which directors should be regulated. These debates touch on underlying questions that permeate the thesis: should directors' actions be judged objectively or subjectively; and should the duty fulfil a function that reflects prevailing norms, or should it set higher standards instead.¹⁵⁰ It is especially as far as the independent non-executive director is concerned, that the duty to monitor the activities of peers and subordinates is of pivotal importance. As Worthington points out, this facet of the duty of care has become 'one of the most crucial aspects of a director's duty. Failures have the potential to lead to enormous corporate losses. Almost all of the modern cases on directors' duty of care concern this particular issue and serve to highlight the magnitude of the problem.'¹⁵¹

Although the duty of care and skill is the most obvious candidate for 'Code based' reforms, it is possible that certain fiduciary duties may be implicated as well - it is specifically the ubiquitous mandate to act in the best interests of the company that comes to mind. In this regard, the company could be taken to refer to a collection of any number of stakeholders, and the mandate may be narrowly or more broadly construed.¹⁵² King IV propagates

¹⁵⁰ See for example: E Norman Veasey 'Should Corporation Law Inform Aspirations for Good Corporate Governance Practices or Vice Versa?' 2001 (149) *University of Pennsylvania Law Review* 2179.

¹⁵¹ Sarah Worthington, 'The Duty to Monitor: A Modern View of the Director's Duty of Care' in F Patfield F (ed), *Perspectives on Company Law: 2* (Kluwer Law International 1997) 181, 194. Consider for example clear failing such as those in the instance of Volkswagen: Raymond Crête 'The Volkswagen Scandal from the Viewpoint of Corporate Governance' 2016 (7) *EJRR* 25.

¹⁵² South African courts have consistently concluded that the interests of the company are the interests of the shareholders present and future *South African Fabrics Ltd v Millman, NO, and Another* 1972 (4) SA 592 at 596. See also: *Harcourt v Eastman* NO 1953 (2) SA 424 (N) at 428 429; *Marshall Industrials Ltd v Khan* 1959 (4) SA 694. For an overview of the stakeholder debate see: Keay A *The Enlightened Shareholder Value Principle and Corporate Governance* (Routledge 2013); Deakin S 'The Coming Transformation of Shareholder Value' (2005) 13(1) *C.G* 11; Deryn Fisher 'The enlightened shareholder - leaving stakeholders in the dark: will section 172(1) of the Companies Act 2006 make directors consider the impact of their decisions on third parties?' (2009) 20(1) *ICCLR* 10; R. Edward Freeman, Andrew C.

without reserve for an approach that is stakeholder inclusive (arguably to a far greater extent than that to which black letter company law has done before). The indirect consequence of an interpretation that takes on board provisions of the code could in turn impact South African law's approach to this so-called 'stakeholder debate'.¹⁵³

The courts have been tasked with the interpretation of the provisions of the Companies Act 71 of 2008. The legislation leads us into uncharted territory not only because it came into operation as recently as seven years ago, but also because it draws inspiration from jurisdictions that South African company law did not traditionally align with. Given all this, the interpretation of the new statutory provisions is especially important. The latest authority from the SA Supreme Court of Appeals favours a 'business like' outcome when interpreting statutes and commercial documents¹⁵⁴ and the Constitutional Court is increasingly placing emphasis on Afro-centric interpretations and notions such as Ubuntu.¹⁵⁵ In light of this, chapter 5 will consider the court's remit in terms of the common law, the Companies Act and the Constitution and will consider whether there is any scope for the application of the King IV.

Wicks and Bidhan Parmar 'Stakeholder Theory and "The Corporate Objective Revisited"' (2004) 15(3) *Org Sci* 364; Anant K Sundaram & Andrew C Inkpen 'The Corporate Objective Revisited' (2004) 15(3) *Org Sci* 350.

¹⁵³ In this regard, Esser and Delport observed that '[t]here has been a discernible movement away from the shareholder supremacy philosophy, but the legal principles underlying this philosophy are entrenched throughout company law and amendments thereto will, at this stage at least, be radical. The use of soft law such as King IV will facilitate this shift in philosophy in a manner that will have the least impact on the philosophies underlying company law. Esser & Delport (n104) 384.

¹⁵⁴ *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) SA 593 (SCA) para 18

¹⁵⁵ Chumo Himonga, Max Taylor and Anne Pope 'Reflections on Judicial Views of Ubuntu' (2013) 16 *PELJ* 171. In this regard King IV notes at 24: This idea of interdependency between organisations and society is supported by the African concept of *Ubuntu* or *Botho*, captured by the expressions *uMuntu ngumuntu ngabantu* and *Motho ke motho ka batho* – I am because you are; you are because we are. *Ubuntu* and *Botho* imply that there should be a common purpose to all human endeavours (including corporate endeavours) which is based on service to humanity.

As society came to terms with juristic persons, debates immersed that centred around the justification for the corporate form. Scholars from various disciplines subsequently started to engage with the inner mechanics of the ‘firm’¹⁵⁶ and especially legal scholars considered the role of the regulator and the extent to which the latter should oversee private ordering within companies.¹⁵⁷ Chapter 6 will consider the theories that have informed regulators (at least those in the Anglo-Saxon context) and have directly or indirectly shaped the corporate law that we know today. The chapter will emphasise the contractarian theory and the agency theory (as explained above). It will consider whether these paradigms might have led the regulatory state (to some extent) to withdraw from establishing ‘effective managerial accountability mechanisms at the micro level’.¹⁵⁸

Any debate centred around the law’s response to incompetence, carelessness or misdirected behaviour on the part of the company director would be incomplete without also considering the reality that action against directors personally is rarely taken. For this reason, chapter 7 will turn to the

¹⁵⁶ The concept is broader than the company but for purposes of this research the terms are used interchangeably.

¹⁵⁷ See for example the following sources engaged with in chapter 6: Attenborough (n 136) 191; Mathew T. Bodie ‘The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm’ (2012) 35 *Seattle U. L. Rev.* 1033; William W. Bratton ‘Self-Regulation, Normative Choice, and the Structure of Corporate Fiduciary Law’ (1993) 61 *Geo. Wash. L. Rev.* 1084; Cheffins *BR Company Law: Theory, Structure and Operation* (Clarendon Press 1997); John C. Jr. Coffee ‘The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role’ (1989) 89 *Colum. L. Rev.* 1618; Michael Galanis ‘Vicious Spirals in Corporate Governance: Mandatory Rules for Systemic (Re)Balancing?’ (2011) 31(2) *Oxford J.Leg.St.* 327; Henry Hansmann & Reinier Kraakman ‘The End of History for Corporate Law’ (2001) 89 *GEO. L.J.* 439; Kraakman and others *The Anatomy of Corporate Law* (n38); Marc T. Moore ‘Whispering Sweet Nothings: The Limitations of Informal Conformance in UK Corporate Governance (2009) 9 *J. Corp. L. Stud.* 95; Moore *Governance in the Shadow* (n79).

¹⁵⁸ Moore *Governance in the Shadow* (n79) 8. The author argues that ‘[l]aw-making functions have been restricted to ‘broad procedural standards and mechanisms’, which provide a facilitative framework for private ordering within individual companies, this has ultimately left corporate participants with a material degree of self-regulatory ‘space’ in which to determine directly, and on an individual firm basis, which substantive accountability norms will govern their ongoing governance relationships with one another.’

issues of accountability and enforcement. The financial crisis and several large-scale corporate scandals following it have shown repeatedly that shareholders in particular, rarely act against directors. If this is the case, any reconfiguration of the duties is rendered moot 'for there is little point in formulating appropriate standards of care if those standards cannot or will not be brought to bear on directors or, indeed, if other methods of controlling competence are likely to be more effective.'¹⁵⁹ The chapter will also discuss voluntary or self-regulation as opposed to statutory regulation and how the one informs the other.¹⁶⁰ These themes relate directly to those discussed in chapter 6 and builds on the arguments it introduces.

Finally, chapter 8 will consolidate the various strands, and given an overview of the research in an attempt to draw clear conclusions and evaluate the questions at the heart of the research.

6 Methodology and Research Parameters

The research is a doctrinal analysis of the law. The research will not include empirical analysis or data collection. The most prevalent sources in the form of statutes, corporate governance codes, relevant reports and expert opinion in the form mainly of scholarly writings such as monographs and

¹⁵⁹ Vanessa Finch 'Company Directors: Who Cares About Skill and Care?' (1999) 55(2) *MLR* 179, 179.

¹⁶⁰ The literature is extensive will be considered in greater depth in Chapter 7. See in general: Vanessa Finch 'Corporate governance and Cadbury: self-regulation and alternatives' (1994) *J.B.L* 51; Saleem Sheikh and William M. Rees 'Corporate governance and corporate control: self regulation or statutory codification?' (1992) 3 *ICCLR* 370; Cadbury (n1) 403 – 405; David Kershaw 'Corporate Law and Self-Regulation (2015) 5 *LSE Law, Society and Economy Working Papers* 4, available online <http://ssrn.com/abstract=3574201>; Ben Pettet 'The combined code: a firm place for self-regulation in corporate governance' (1998) 13 *J.I.B.L.R* 394; Tricker (n5) chapters 5 & 6; Jean Jacques du Plessis and others *Principles of Contemporary Corporate Governance* (3rd edn Cambridge UP 2015) chapter 5; Roman Tomasic and Folarin Akinbami 'Towards a new corporate governance after the global financial crisis' (2011) 22(8) *ICCLR* 237.

academic articles will be consulted. Although the thesis will consider the interactions between South Africa's corporate governance code and legislation, not all of King IV is discussed and analysed and a specific chapter is not devoted to the contents of the Code. The reason for this is the fact that there is much of King IV that will in no way alter or impact the interpretation and application of the Companies Act. Furthermore, the research question focusses specifically on the impact that an interaction between the Code and the Act might have on how directors' duties are interpreted and applied. As such, the matter was approached by analysing the duties that may be impacted in turn, with reference to the Code as and when appropriate as opposed to a wholesale discussion of provisions that are not directly pertinent.

7 Conclusion

It is no exaggeration to say that the threats and challenges that the world faces today are unprecedented in their complexity and global impact. National governments are often at a loss, facing matters as diverse as climate change, wide scale political unrest and war, mass migration and the rapid and continued ascent of technology. But it is not only nation states that find themselves ill prepared in the face of these risks. The company must rise to the challenge in new and surprising ways, and prove its agility if it is to continue to flourish. Almost sixty years ago, Berle summarised that the corporate form presents:

A commercial instrument of formidable effectiveness, feared because of its power, hated because of the excesses with which that power was used, suspect because of the extent of its political manipulations within the political State, admired because of its capacity to get things done. From the turn of the twentieth century to the present, nevertheless, its position as a major method of business organisation has been assured. Although it was abused, no substitute form of organisation was found.

The problem was to make it a restrained, mature and socially useful instrument.¹⁶¹

Hundreds of thousands of pages of reports, recommendations, statutes and governance codes have since seen the light and yet countries worldwide still battle with a problem that is decades old. Ensuring that our companies are 'restrained, mature and socially useful instruments' remains a global challenge - and South Africa is no exception.

South Africa is a developing economy. Poor economic growth and socio-economic inequality hamstring development. Robust corporate entities that can weather a multitude of challenges are essential to future growth and stability.¹⁶² The benefits of sound corporate governance can hardly be understated and this is the case not only for listed entities but for small to medium enterprises as well.¹⁶³ Although the first King Code of Corporate Governance was introduced decades ago, a culture of good governance has not been entrenched and many corporates are still just 'ticking boxes'. The courts have taken a more robust approach and are hinting at an interpretation of directors' duties that take onboard principles set out in the King Code of Governance. The relatively opaque nature of especially the duty of care and skill has already been highlighted above. The interaction between these duties and the voluntary Corporate Governance Codes is as ill defined.

The implications of this are manifold and especially relevant to how the law treats the independent non-executive director – a stalwart of corporate

¹⁶¹ AA Berle Foreword in *The Corporation in Modern Society* (Harvard UP 1959) X.

¹⁶² See Johan J. Henning, 'Reforming Business Entity Law to Stimulate Economic Growth Among the Marginalised: The Modern South African Experience' (2002) 91 *KY. L.J.* 773; Johan J. Henning 'Close Corporation Law Reform in Southern Africa' (2001) 26 *J. CORP. L.* 917.

¹⁶³ Henning *Reforming Business Entity Law* (n158); Henning, *Close Corporation Law* (n158).

governance. The thesis considers both the normative or policy consideration that are at play as well as the technical and constitutional matters that arise from such an approach. The likely conclusion will be that there is some role for the Codes in formulating the duties but that several caveats apply. What waits at this intersection between hard and soft law: a stumbling block, a stepping stone, or both?

CHAPTER 2

THE INDEPENDENT NON-EXECUTIVE DIRECTOR: THE ORIGINS OF THE OFFICE, CURRENT REGULATION AND PERSISTENT CHALLENGES

If you have five directorships it is total heaven, like having a permanent hot bath.

No effort of any kind is called for. You go to a meeting once a month in a car supplied by the company, you look grave and sage, and on two occasions say, 'I agree,' say 'I don't think so' once, and if all goes well you get £500 a year.¹

1 Introduction

The aim of this research is to consider the potential role of King IV in the interpretation of common law and statutory directors' duties in South African law. To do so, the duties themselves require scrutiny, as do the policies and theories that drive and inform their continued development, the legal constraints faced by the courts in their application and the mechanisms aimed at ensuring accountability in the boardroom. However, before turning to these matters, the analysis will consider the role of the independent non-executive director - a staple of voluntary corporate governance codes and subject to the duties in question.²

Despite little empirical evidence of their value or contribution,³ the premise that non-executive directors acting independently from management is

¹ Lord Boothby as quoted by: *Chamberlain*, "Why Its Harder and Harder to Get a Good Board", *Fortune*, Nov. 1962, at p. 109 as cited by A J Boyle 'Company Law and the Non-Executive Director – The USA and Britain Compared' (1978) 27 *Int. Com. LQ* at 490.

² It bears repeating that the duties apply to executive and non-executive directors alike and that, technically, the duties are in place to regulate the office of both the executive and non-executive director.

³ W Ringe 'Beyond "Independent" Directors: A Functional Approach to Board Independence' (2006) 119 (5) *HarvLRev* 1553 where the author gives an overview

essential to the integrity of the company board has driven much of the corporate governance agenda for decades, and the view seems to ‘gain momentum after each wave of scandals’.⁴ In fact, as an ostensible response to agency dilemmas⁵ ‘the need for active, independent boards has become conventional wisdom’⁶ and (perhaps hyperbolically) those who challenge or oppose the institution of the independent director risk being labelled ‘heretics’.⁷ Nothing illustrates this better than the status quo in the United States, where governance activists propagate for boards on which independent directors make up a ‘substantial majority’.⁸

While it is true that outside the US the embrace of the independent non-executive may have been more lukewarm, one could hardly dispute the fact that the independent non-executive plays a central role in corporate

of the evidence at page 31. See also Du Plessis JJ and Others *Principles of Contemporary Corporate Governance* (4th edn Cambridge University Press 2018) where the authors discuss the following conflicting studies: Bernie Fraser *Board Governance of Not for Profit Superannuation Funds* (16 February 2017) which concluded that independent directors would not necessarily deliver improved governance; Peter L Fischer and Marc-Oliver Swan, ‘Does board independence improve firm performance? Outcome of a quasi-natural experiment’ (2013) 1 *SSRN Electronic Journal* DOI: 10.2139/ssrn.2312325 available online at <http://static.squarespace.com/static/53830acee4b0b1911ba0b52e/t/53f420a6e4b027df2521861d/1408508070374/SSRN-id2312325.pdf> [accessed on 09/08/2019] which found no link between independent non-executive directors and firm performance in the Australian context; cf Kathy Fogel, Liping Ma and Randall Morck ‘Powerful independent directors’, European Corporate Governance Institute (ICGI) available online at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2377106&rec=1&srcabs=2222783&alg=1&ps=2 [accessed on 19/06/2019] which concluded that ‘powerful’ independent directors are in fact better able to hold CEO’s accountable as they have improved access to information and greater credibility.

⁴ Alessandro Zattoni and Francesca Cuomo ‘How Independent, Competent and Incentivized Should Non-Executive Directors Be? An Empirical Investigation of Good Governance Codes’ (2010) 21 *Br. J. Manag* 63.

⁵ See chapter 6 text to notes 84 - 102 for an overview and criticisms of the agency theory.

⁶ Ringe ‘Beyond “Independent” Directors’ (n3) 1553; Suzanne Le Mire ‘Independent Directors: partnering expertise with independence’ (2016) 16(1) *J. Corp. Law Stud.* 1.

⁷ Usha Rodrigues ‘The Fetishization of Independence’ (2008) 33 *J.Corp.L.* 457.

⁸ Rodrigues (n7) 457.

governance regimes far and wide.⁹ Considering this, it may come as a surprise that the exact meaning of ‘independence’ in the context of the corporate board remains somewhat of a mystery. Expectations regarding the role and remit of the independent non-executive also remain far from settled, leading to what has been called an ‘identity crisis’¹⁰ on the part of the independent non-executive.

Trying to come to grips with the current debate around independence requires insight into a established political, legal and theoretical discourse and it soon becomes clear that ‘regulators, commentators, and courts have all used ‘independence’ to mean different things at different times for different reasons.’¹¹ Critics also warn that regulators and corporate reformers should refine definitions of independence to address the conflicts they seek to regulate, and more importantly should not lose sight of the fact that independent directors are actually only useful in instances where a conflict exists in the first place. In other words, that independence should be a means to an end and should not become an end in itself.¹²

Chapter 1 introduced the various mechanisms seeking to regulate the conduct of directors with the eye on improving corporate performance and sustainability. As mentioned, apart from more traditional legal duties, the emergence of self-regulatory codes of governance have had a significant

⁹ See for example in the UK: FRC, *The UK Corporate Governance Code* (April 2016) available online at <https://www.frc.org.uk/getattachment/ca7e94c4-b9a9-49e2-a824-ad76a322873c/UK-Corporate-Governance-Code-April-2016.pdf>; in Australia: *ASX CG Principles and Recommendations* (2014) 16; and in South Africa: Institute of Directors *King IV: Part 5.3, Recommended Practice 8*.

¹⁰ Ringe ‘Beyond “Independent” Directors’ (n3) 1553.

¹¹ Ringe ‘Beyond “Independent” Directors’ (n3) 1553.

¹² Rodrigues (n7) 447. See in general also: Ringe ‘Beyond “Independent” Directors’ (n3) 1553; Sweeney-Baird, M ‘The role of the non-executive director in modern corporate governance’ (2006) 27(3) *Co Law* 67; Victor Brudney ‘The Independent Director: Heavenly City or Potemkin Village’ (1982) 95 *HarvLRev* 597. See also below at text to notes 96 – 127.

impact on the corporate landscape. These codes emphasise responsibility and accountability at board level, and focus to varying degrees on the role of the independent non-executive director in ensuring good governance.¹³

This chapter will elaborate on some of these themes. Firstly, the term ‘independent non-executive director’ will be defined both in general and for purposes of this thesis. Some background will show how the office became the ubiquitous feature of the company board of directors that we have come to know. The chapter will then deal briefly with the challenges faced by independent non-executive directors and overview debates surrounding the value of the independent non-executive as a custodian for corporate governance. Following this the various mechanisms that seek to regulate the independent non-executive director will be considered with emphasis on the South African context.

The analysis serves as background to the debates that surround the appropriate and effective regulation of directors which will be discussed in depth later in this thesis. The core research question that this contextual analysis speaks to, is whether more robust interaction between the governance codes and black letter law is notionally or conceptually desirable. This can only be considered in light of a functional understanding of the intricacies of the office in question subject to the regulation being proposed. The aim of this chapter is to introduce the reader to the salient concepts and offer an overview of the most prominent discourse pertaining to them.¹⁴

2 Background

¹³ See note 9 above and examples mentioned.

¹⁴ For further analysis see: Harald Baum ‘The Rise of the Independent Director: A Historical and Comparative Perspective’ Max Planck Private Law Research Paper No. 16/20; Boyle (n1) 487; Brudney (n12) 597.

When considering the independent non-executive director's rise to prominence, it is impossible to avoid mention of the history and development of American corporate governance as this is where the concept had its genesis. Different driving forces led to the phenomenon setting root in British and subsequently in continental European corporate culture,¹⁵ but there is no doubt that many of the fundamentals of the independent board as monitor were informed by American principles.¹⁶ The chronology of the rise of the independent monitoring board in America must, however, be considered bearing in mind that America and the United Kingdom (and by extension South Africa) have very different contexts as far as institutions and regulation are concerned.¹⁷ For example, although both jurisdictions suffer from relatively passive shareholders, Britain is on the whole perceived as placing shareholders in a more powerful position vis-a-vis the board of directors, when compared to the United States.¹⁸ Secondly, as briefly explained in chapter 1, corporate governance is regulated via mandatory law in the United States whereas in the United Kingdom the Companies Act 2006 does little to regulate matters related to the structure and internal functioning of company boards. These aspects are instead, dealt with in the company constitution¹⁹ and by means of contractual agreements with individual directors,²⁰ monitored on a comply or explain basis as was mentioned in chapter 1. In the tradition of English law, the South African legislation tends also to deal in broad strokes with certain minimum

¹⁵ Baum (n14) 22.

¹⁶ Cheffins Brian R 'The Rise of Corporate Governance in the UK: When and Why' (2015) 68 *Current Legal Problems* 387 at 389.

¹⁷ This caveat applies equally when considering the South African context. It bears mention that the United States and the United Kingdom did traditionally have some things in common as well. As Boyle notes, both jurisdictions firmly recognise a separation between ownership and management, and in both countries companies often exist as groups of subsidiaries with the main apex of corporate power in the main board of the primary holding company. See: Boyle (n1) 488.

¹⁸ Baum (n14) 22.

¹⁹ Paul L Davies & Sarah Worthington *Gower's Principles of Modern Company Law* (Sweet & Maxwell 2016 10th ed) 387.

²⁰ Sweeney-Baird (n12) 69.

requirements pertaining to the board and its proper functioning, and generally leaves the minutiae of its regulation to companies themselves. This high-level regulation of the board of directors can likely be attributed to South African law's initial and continuing kinship with English law.²¹ Regulatory restraint also may be due to the belief that corporate law is essential private in nature and that it is best left to the 'parties' of the corporate contract to determine how best to run the entity, and the fact that English company law has its roots in partnership law as explained above.²²

3 Definitions and Development

The South African Companies Act 71 of 2008 defines 'director' as:

'[A] member of the board of a company, as contemplated in section 66,²³ or an alternate director²⁴ of a company and includes any person occupying the position of a director or alternate director, by whatever name designated...'²⁵ The definition²⁶ is broad enough to include those acting as directors without having been formally appointed (so-called 'de facto directors')²⁷ but clearly makes no distinction between executive and non-

²¹ See chapter 1 at text to note 122.

²² See discussion in chapter 6.

²³ Section 66 of the Companies Act deals with the appointment and/or election of directors amongst other matters.

²⁴ An 'alternate director' is defined as "a person elected or appointed to serve, as the occasion requires, as a member of the board of a company in substitution for a particular elected or appointed director of that company." See: Companies Act 71 of 2008, s 1.

²⁵ Companies Act 71 of 2008, s 1.

²⁶ The definition (in both the South African and the UK Companies Acts) raises many matters not directly relevant to the research. Other than a brief mention below these issues will not be dealt with in greater depth. For further analysis see: Cassim and others *Contemporary Company Law* (n83) 404 – 411; Henochsberg *on the Companies Act 71 of 2008* (Issue 18 2018); Davies and Worthington (n178) 386.

²⁷ Cassim and others *Contemporary Company Law* (n83) 404, 408. The definition in the South African Companies Act seems not to include persons known as 'shadow directors' although individuals acting as shadow directors may be considered "prescribed officers" for purposes of the Act, in which case several provisions

executive directors.²⁸ It also makes no reference to director independence; indeed, no reference to an 'independent director' in the general sense, is found anywhere else in the legislation. The definition found in the Companies Act 2006 is similar,²⁹ and seems to support the idea that, amongst others, the general statutory duties could be applied to de facto directors also.³⁰

The Companies Act 2006 does require all companies to have a board of directors in place,³¹ and stipulates the minimum number of directors required for various types of companies.³² Apart from this, the legislation is not specific or prescriptive, leaving the exact composition of the board to each individual company. As Davies and Worthington point out, the Companies Act 2006 largely leaves it up to each company to determine the role of the board in its constitution.³³ The fact that the division of power can thus be arranged privately by the members of the company via its constitution and employment agreements with individual directors likely harks back to the fact that the roots of British company law can be found in partnership, with the partners having great freedom to arrange their

(including sections 76 and 77 which deal with directors' standards of conduct and liability will apply to them). See: Kathy Idensohn 'The meaning of 'prescribed officers' under the Companies Act 71 of 2008' (2012) 129(4) *South African Law Journal* 717 – 735; Kathy Idensohn 'The Regulation of Shadow Directors' (2010) 22(3) *SA Merc LJ* 326 – 345. The Companies Act 2006 in contrast, defines a shadow director as 'a person in accordance with whose directions or instructions the directors of the company are accustomed to act' and deals expressly with the application of any provisions in relation to shadow directors.

²⁸ See also: Cassim and others *Contemporary Company Law* (n83) 411.

²⁹ Section 250 of the Companies Act defines 'director' as 'any person occupying the position of director, by whatever name called.'

³⁰ Davies and Worthington (n481). In fact, it has long seemed uncontentious that the general duties did apply to de facto directors under English law, although the factual question of whether an individual can be considered a de facto director has been less settled. See for example: *Re Canadian Land Reclaiming and Colonizing Co* (1880) 14 Ch. D. 660; *Secretary of State for Business, Innovation and Skills v Chohan* [2013] EWHC 680 (CH); *Vivendi SA v Richards* [2013] EWHC 3006.

³¹ A single tier board seems to be assumed although not expressly required, see s 154.

³² S 155.

³³ Davies and Worthington (n178) 481.

internal affairs.³⁴ This arrangement goes some way in facilitating the use of a single act to govern companies that vary greatly in size and structure, and jurisdictions with more prescriptive statutory regimes tend to have separate pieces of legislation to regulate smaller entities.³⁵ The authors further note that:

It is also a point of some theoretical (even ideological) importance: the directors' authority is derived from the shareholders through a process of delegation via the articles and not from the separate and free-standing grant of authority from the State. This helps to underline the shareholder-centred nature of British company law.³⁶

South African law has broken with this tradition, and the Companies Act 2008 now expressly states that 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 Incorporate provides otherwise.'³⁷ The board's authority is therefore now derived from statute and not granted by the shareholders as was previously the case.³⁸ It is perhaps ironic that the very piece of legislation introducing this change simultaneously abolished South Africa's Close Corporations Act³⁹

³⁴ See chapter 1, text to note 35.

³⁵ Davies and Worthington (n178) 481.

³⁶ Davies and Worthington (n178) 481 *cf* Susan Watson 'The significance of the source of the powers of boards of directors in UK company law' (2011) 6 *JBL* 597 where the author questions this view, and argues that 'the allocation of powers to boards through the constitution is most likely an anomaly brought about by the drafters of the original Joint Stock Companies Act 1856 using as a precedent existing deeds of settlement. Accordingly, it is suggested that no significance at all should be attached to this point of difference in UK company law and no conclusions about the legal relationship between boards and shareholders drawn from the allocation of powers being in the constitution rather than the statute.' See also comments below at chapter 8.

³⁷ Companies Act 71 of 2008, s 66(1).

³⁸ Cassim refers to this 'original' authority that the statute now grants as a 'concession to reality by acknowledging that the *raison d'être* for the appointment of a board of director is the management of the company's business'. Cassim and others *Contemporary Company Law* (n83) 403.

³⁹ 69 of 1984.

which catered for smaller entities and gave exactly the autonomy to regulate internally that Davies and Worthington refer to above. The original authority granted to the board by the Companies Act 2008 in this sense seems anathema to the flexibility required when a single piece of legislation seeks to regulate companies varied in size and complexity. In this regard however, it must be said that although the paradigm shift towards statutory board authority may in the long term affect the jurisprudential approach to South African company law, the practical manifestations of its English law heritage have remained largely intact.⁴⁰ That is, while directly granting authority, the statute remains generally permissive and allows the members of the company by means of the constitution, to determine privately what exactly its board should look like and what its role should be.⁴¹

The consideration of the legislation above makes it clear that, as far as both South African and English law is concerned, the independent non-executive director is not a creature of statute - on paper that is, there is no difference between the executive and non-executive director.⁴² This then begs the question; how and when did the independent non-executive director become a central feature of company boards all over the world, and what exactly is it?⁴³

a General Historical Overview

As the overview in Chapter 1 showed, seventeenth century trading companies in Britain (such as the East India Company) were structured to resemble modern joint-stock companies. Companies were increasingly

⁴⁰ It is interesting to note the similarities between the wording of section 66(1) of the Companies Act 71 of 2008, and the default provision found in article 3 of the UK's model articles: 'Subject to the articles, the directors are responsible for the management of the company's business, for which purpose they may exercise all the powers of the company.'

⁴¹ See also notes in this regard in chapter 8.

⁴² Sweeney-Baird (n12) 69.

⁴³ See note 12 and sources cited.

being transformed into entities that allowed for passive investment by the general public.⁴⁴ As one might expect, the boards of American companies initially mimicked the British tradition, and as colonies generally tended to adopt the institutions of their European colonisers, the board of directors was adopted as a corporate governance tool in numerous other jurisdictions as well.⁴⁵

As chapter 1 explains, directors of the earliest companies tended to be heavily invested in the entities that they served. There were hardly any doubts that they would tend to act to the benefit of the company as this would align with their own interests, and a supervisory or monitoring board was superfluous.⁴⁶ As joint-stock companies flourished in the eighteenth and nineteenth century,⁴⁷ and became an increasingly popular and attractive investment vehicle for ordinary citizens, investors became more dispersed and in the face of this more pronounced separation between ownership and control, it was initially assumed that companies would be managed by their boards of directors.⁴⁸

This harks back to what (in America) was called the ‘received legal model’ of the corporate board, namely that ‘the board, theoretically elected by the shareholders, selects the officers ... sets policy and generally manages the business.’⁴⁹ But as Boyle pointed out some 40 years ago ‘it hardly needs to

⁴⁴ Baum (n14) 9.

⁴⁵ Baum (n14) 9, where the author points out that even ‘Japan, which was never colonized, regarded the modern joint-stock corporation with its board as a superior form of enterprise for establishing and conducting business. Immediately after the Meiji Restoration of 1868, the Japanese government began to promote the introduction of a company system, and the first Japanese banks had to be organized as joint-stock companies by decree in 1876.’

⁴⁶ Baum (n14) 8. The author notes a parallel development of joint-stock companies and corporate boards in Continental Europe, with the Dutch East India Company being perhaps the most notable example.

⁴⁷ Partly spurred by the creation of the separate legal entity and the phenomenon of limited liability which could shelter investors.

⁴⁸ Baum (n14) 10.

⁴⁹ Boyle (n1) 489, where the author cites W Cary, *Corporations-Cases & Materials* (4th ed Foundation Press 1969) 150.

be said that in any serious sense this is not possible for the board of any large public corporation'.⁵⁰ In fact, even the idea that the board in this traditional sense was truly equipped to weigh in on long-term policy and more general strategy was often completely unrealistic.⁵¹

This reality manifested as early as the nineteenth century, as an organic split developed between professional managers acting as executive directors and those offered a seat on the board with no managerial functions attached.⁵² In the case of a well-run company, these 'guinea pig' directors were largely perfunctory,⁵³ and were in fact often appointed from the ranks of the nobility or, in the case of the United States, celebrities or retired generals to add lustre to the board and to attract investment, not because they had any particular skills to speak of.⁵⁴

b The Non-Executive Director in American Law and Practice

As corporate scandals rocked the United States in the early twentieth century, classic agency dilemmas became more pronounced and led to the first calls for some form of a monitoring board that could actually oversee the actions of management.⁵⁵ Regardless, boards continued to play a largely

⁵⁰ Boyle (n1) 489.

⁵¹ Boyle (n1) 489.

⁵² Brenda Hannigan 'Board failures in the financial crisis - tinkering with codes and the need for wider corporate governance reforms: Part 1' (2011) 32(12) *Co Law* 363, 364; Baum (n14) 10.

⁵³ Boyle (n1) 499 where the author quotes a rather scathing critique by Alex Rubner from his work *The Ensnared Shareholder* (Macmillan 1965) 56: 'When scrutinizing the composition of the boards one must perforce conclude that many of the members are not to be taken seriously. The appointment of " guinea-pig directors" originated in Britain, where nobles, drawing fees in guineas, lent their names to corporations; in order to dupe the public, to whom the presence on the board of a member of the aristocracy symbolized business acumen and/or respectable management.'

⁵⁴ Boyle (n1) 499. See also the discussion in chapter 3 below at text to note

⁵⁵ Jeffrey N Gordon 'The Rise of Independent Directors in the United States' 1950 – 2005: Of Shareholder Value and Stock Market Prices' (2007) 59 *Stan.L.Rev* 1465;

passive role in the United States, with members usually nominated by the CEO, with the latter often also chosen as chairman of the board. This state of affairs naturally left the board relatively impotent; essentially acting at the behest of the CEO, and the autonomy of management was all but taken for granted.⁵⁶

Change was finally sparked in the 1970's by the collapse of Penn Central,⁵⁷ and fallout from the Watergate scandal⁵⁸ which propelled the issue into the public domain and main stream politics.⁵⁹ An academic publication also had some impact,⁶⁰ in the form of Melvin Eisenberg's famous '*The Structure of the Corporation*'⁶¹ where the author contended that monitoring senior management was the board's primary mandate. The 1970's thus saw 'managerial elites [make] significant concessions'⁶² and by the time a series of hostile takeovers struck the United States in the 1980's the monitoring board had largely become accepted practice. Based on this, Delaware courts

Baum (n14) 11, where the author refers to the famous example by author William O. Douglas: 'Directors Who Do Not Direct' (1934) 47 *Harv. L. Rev.* 1305.

⁵⁶ Baum (n14) 11; Boyle (n1) 487; Noyes E Leech & Robert H Mundheim 'The Outside Director of the Publicly Held Corporation' (1976) 31(4) *Bus Law* 1799, 1811; Tricker (n5) 8.

⁵⁷ It later transpired that the directors of this major railway company knew precious little about the company's affairs and had done very little to educate themselves. For an overview of the scandal what was at the time the biggest bankruptcy in American history see: Stephen Salsbury *No Way to Run a Railroad* (McGraw-Hill 1982); Robert Sobel *The Fallen Colossus* (Weybright and Talley 1977).

⁵⁸ Various illegal campaign contributions and bribes came to light following the scandal. There have been numerous reviews of the events. See for example: Michael Schudson 'Notes on Scandal and the Watergate Legacy' (2004) 47(9) *Am.B.Sci* 1231; Keith Olson *Watergate: the presidential scandal that shook America* (University Press of Kansas 2003); Michael Schudson *Watergate in American memory: how we remember, forget, and reconstruct the past* (BasicBooks 1992).

⁵⁹ Baum (n14) 13; Boyle (n1) 493.

⁶⁰ Baum (n14) 13

⁶¹ Melvyn Eisenberg *The Structure of the Corporation: A Legal Analysis* (Little, Brown & Co. 1976).

⁶² Baum (n14) 13.

tended to defer to the decision of the board provided that it functioned along these newly accepted lines.⁶³

Summarising these developments in 1978, Boyle observed that the increased focus on the duties and real powers of the North American non-executive, was part of an attempt to introduce a 'new institutional check (into the traditional, corporate structure) in order to prevent corporate abuses and plain mismanagement. It has been seen as a type of internal self-regulation designed to prevent such abuses arising in the first place – as opposed to seeking remedies to cure them after the event (with an attendant blaze of publicity)'.⁶⁴

The spate of corporate scandals during the early 2000s⁶⁵ was largely blamed on failings on the part of external gatekeepers but nevertheless exposed the shortcomings of a governance system that by then had fully embraced the independent board as monitor.⁶⁶ In spite of this lawmakers in the United States remained committed to the precept and responded by requiring increased independence on the part of company boards.⁶⁷

In fact, by 2010 boards in the United States ostensibly gave the notion of director independence such credence that companies opted voluntarily for so-called 'super-majority' boards, with only a single director (usually the CEO) not being an independent director.⁶⁸

⁶³ Baum (n14) 15; Rodrigues (n7) 456. See also chapter 6 and 7 for additional observations regarding the judiciary's deference to the board at Chapter 6 text to notes 105 – 108 and Chapter 7 page text to note 80 onwards.

⁶⁴ Boyle (n1) 487.

⁶⁵ See chapter 1 at note 3 and sources cited.

⁶⁶ Baum (n14) 15; Rita Esen 'Managing and monitoring: the dual role of non-executive directors on U.K and U.S boards' (2000) 11(6) *ICCLR* 202; 203. And see: Gordon (n55) 1465, where the author attributes the prevalence of the independent director in the US context to an increased emphasis on shareholder primacy.

⁶⁷ Baum (n14) 16; Gordon (n55) 1465.

⁶⁸ Baum (n14) 17 emphases added; Rodrigues (n7) 457.

c The Non-Executive Director in English and European Law and Practice

Across the pond, the United Kingdom embraced the monitoring board at a much later stage, and it was at first spurred by industry as opposed to government intervention.⁶⁹ Change was prompted by the publication of the Cadbury Report in 1992.⁷⁰ As mentioned, the report, prepared by the Committee on Financial Aspects of Corporate Governance under the chairmanship of Sir Adrian Cadbury, was influential and quickly gained international attention.⁷¹ As far as the United Kingdom is concerned, it effectively represents the beginning of the corporate governance movement.⁷² The report singled out dominant company CEO's as a specific threat to good corporate governance and in response made various suggestions to counter this balance of power such as the inclusion of a sufficient number of independent non-executive directors to the board.⁷³ The original report was subsequently reviewed a number of times,⁷⁴ before emerging as the UK Corporate Governance Code in 2010,⁷⁵ which recommended that 'the board and its committees should have the appropriate balance of skills, experience, independence and knowledge of

⁶⁹ See for example the PRO NED project backed by the Bank of England, the Confederation of British Industry and the Institutional Shareholders' Committee and The Stock Exchange. EJ Jacobs 'Non-executive directors' 1987 *JBL* 269, 269.

⁷⁰ David Walker *A review of corporate governance in UK banks and other financial industry entities: Final recommendations* (2009) available online at https://webarchive.nationalarchives.gov.uk/+/www.hm-treasury.gov.uk/d/walker_review_261109.pdf. And see: Esen 'Managing and Monitoring' (n66) 203.

⁷¹ Baum (n14) 22. The Cadbury Report is considered one of the main catalysts for the development of a Corporate Governance Code in South Africa. See chapter 1 note 104.

⁷² Davies and Worthington (n178) 392.

⁷³ Davies and Worthington (n178) 391.

⁷⁴ For an overview of these developments see: Hannigan (n52) 364; Baum (n14) 22.

⁷⁵ See also Chapter 1 note 104 for further comments regarding the history and development of both the UK and the SA codes of governance.

the company to enable them to discharge their respective duties and responsibilities effectively'.⁷⁶

The Higgs Review, published in January 2003, considered the role of the non-executive director and offered detailed guidance with the eye on avoiding further 'Enron – like' disasters.⁷⁷ The review led to a 'radical reshaping of the board' with an increased emphasis on a more dynamic role for the independent non-executive director.⁷⁸ Following this, a new-found emphasis on skill and expertise, and modified approach to independence were introduced in response to the apparent failings on the part of independent non-executive directors identified by the Walker Review which was commissioned to investigate the issue following the 2007/2008 financial crisis.⁷⁹ The reforms following the financial crisis show a departure from a strict approach to the more absolutist approach to independence adhered to by the United States. This largely remains the case even after the major losses brought about by the events of 2007/2008, with independent directors having apparently 'achieved an almost cult-like status as a magic cure for a variety of corporate governance ills.'⁸⁰

As outlined in chapter 1, following the lead of the Cadbury Report, most European Union Member states now boast similar corporate governance codes, operating on a comply or explain basis. It also gradually became a European standard that boards of directors should consist of at least some

⁷⁶ Main Principle B, Corporate Governance Code 2014. The Principle is the same in the 2010, 2012, 2014, and 2018 editions of the CGC.

⁷⁷ Derek Higgs *Review of the role and effectiveness of non-executive directors* (2003) available online at <https://web.archive.org/web/20080726222758/http://www.berr.gov.uk/files/file23012.pdf> And see: Paul Burke 'The Higgs Review' (2003) 24(6) *Co Law* 162.

⁷⁸ Burke (n77) 162.

⁷⁹ David Walker *A review of corporate governance in UK banks and other financial industry entities: Final recommendations* (2009) available online at https://webarchive.nationalarchives.gov.uk/+/www.hmtreasury.gov.uk/d/walker_review_261109.pdf.

⁸⁰ Baum (n14) 3.

independent non-executive directors.⁸¹ A non-binding 2005 Recommendation by the European Commission⁸² closely follows what was then the UK Combined Code and calls for ‘an appropriate balance of executive/managing and non-executive/supervisory directors such that no individual or small group of individuals can dominate decision making’.⁸³ The financial crisis of 2008 sparked stricter regulation and following a 2014 Directive it is now mandatory for a majority of independent directors and an independent chair to populate audit committees of public interest companies.⁸⁴

d The Non-Executive Director in South African Law and Practice

As the overview of the statutory definitions above shows, South Africa’s Companies Act does not differentiate between executive and non-executive directors, nor does it demand that any members of the board are in any way independent. The predecessors of the 2008 Act likewise made no such distinctions, although it is clear from case law that there have been distinctions between executive and non-executive directors in practice for

⁸¹ Baum (n14) 3.

⁸² Commission Recommendation (2005/162/EC) of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board, OJ L 52/51 available online at <https://publications.europa.eu/en/publication-detail/-/publication/1e430f30-7d2f-4036-8ee4-f302913bdbff> [accessed on 03/09/2018].

⁸³ Section 3.1; Commission Recommendation (2005/162/EC) of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board, OJ L 52/51 available online at <https://publications.europa.eu/en/publication-detail/-/publication/1e430f30-7d2f-4036-8ee4-f302913bdbff> [accessed on 03/09/2018].

⁸⁴ Directive 2014/56/EU of the European Parliament and of the Council of 16 April 2014 amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts, [2014] OJ L158/196 available online at <https://publications.europa.eu/en/publication-detail/-/publication/1e430f30-7d2f-4036-8ee4-f302913bdbff> [accessed on 03/09/2018].

some time, and debate about whether or not this practical distinction should be recognised by the courts.

In the landmark case of *Fisheries Development Corporation of SA Ltd v Jorgensen and Another*⁸⁵ Morgan J confirmed that the extent of the duty of care that a director owes his/her company would depend on the nature of the company's business and the obligations of that director. The court relied specifically on the famous English case of *In re City Equitable Fire Insurance Co.*⁸⁶ as basis for this and the concomitant conclusion that one must therefore distinguish between the executive and non-executive director. The latter, according to the court, has duties that are of an intermittent nature, to be exercised when attending meetings from time to time – although no obligation to attend all meetings exists.⁸⁷

As far as the non-executive director is concerned, Morgan J remarked further that: 'Nowhere are his duties and qualifications listed as being equal to those of an auditor or accountant. Nor is he required to have special business acumen or expertise, or singular ability or intelligence, or even experience in the business of the company'.⁸⁸ However, a director's actual knowledge or skill set will be used as a measure when judging his actions. It is perhaps notable that the case was decided before the corporate governance movement gained traction and as such, before the office of the independent non-executive director was imbued with the responsibilities that now define it.

In the subsequent decision of *Howard v Herrigel*,⁸⁹ Goldstone AJ reverted to a more traditional approach, commenting that: 'it is unhelpful and even misleading to classify company directors as "executive" or "non-executive"

⁸⁵ 1980 (4) SA 156 (W).

⁸⁶ [1925] Ch 407.

⁸⁷ At page 165 par [H].

⁸⁸ At page 166 par [A]. The court relies on *In re Brazilian Rubber Plantations and Estates Ltd* (1911) 1 Ch 425 at 437, to support its conclusion.

⁸⁹ [1991] 2 All SA 113 (A).

for purposes of ascertaining their duties to the company or when any specific or affirmative action is required of them.⁹⁰ The court pointed out that statute recognised no distinction between executive and non-executive directors and reiterated that, at common law, accepting an appointment as a director renders one a fiduciary in relation to the company with a concomitant obligation to display the utmost good faith regardless of whether one is an executive or a non-executive director. Although one must necessarily take into account the fact and circumstances of each case when applying this general rule to any particular incumbent director, Goldstone JA concluded that ‘it is not helpful to say of a particular director that, because he was not an “executive director”, his duties were less onerous than they would have been if he were an executive director. Whether the inquiry be one in relation to negligence, reckless conduct or fraud, the legal rules are the same for all directors.’⁹¹ Whether this approach remains viable in light of the evolved role of the non-executive director is entirely debatable.

It can be said that the distinction between the executive and non-executive director became a more formalised industry staple with the introduction of the first King Code on Corporate Governance in 1994. Recently, King IV reconsidered its approach to the independent non-executive in line with international trends. It requires that the ‘governing body should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.’⁹² Like its UK counterpart, it stipulates that the

⁹⁰ At page 130.

⁹¹ At page 131. These observations of the court must prompt one to ask whether this approach is still valid today given the very different roles played by executive and non-executive directors, and indeed the key role played by the independent non-executive director.

⁹² King IV, Principle 7.

governing body should comprise a majority of non-executive members, most of whom should be independent.⁹³

Of particular concern in the South African context is the fact that directors are often 'over boarded'.⁹⁴ Various reasons are given for this – such as a lack of qualified candidates – and it arguably leaves industry with the complex responsibility to overcome the dilemma. The phenomenon is not unique to South Africa however,⁹⁵ and is also merely one of the concerns that have been raised in relation to the role and efficiency of the independent non-executive director.

4 Challenges and Criticisms

Perhaps the most apparent practical, or technical challenge when considering director independence is the opaque nature of the concept itself.⁹⁶ In fact, for a concept as ubiquitous in such a variety of regulatory

⁹³ King IV, Recommended Practice 8. A 'substance-over-form' approach is endorsed for purposes of determining whether a director is independent. See Recommended Practice 28.

⁹⁴ Innoxico. 2013. The Innoxico Director Singularity Index: Research Report. Available online at: [http://www.ey.com/Publication/vwLUAssets/The_Innoxico_Director_Singularity_Index_-_2013_Research_Report/\\$FILE/Innoxico.pdf](http://www.ey.com/Publication/vwLUAssets/The_Innoxico_Director_Singularity_Index_-_2013_Research_Report/$FILE/Innoxico.pdf). [Accessed 4 April 2019]. See also: Nadia Mans-Kemp, Suzette Viviers & Sian Collins 'Exploring the causes and consequences of director overboardedness in an emerging market' (2018) 15 *J&G* 210, where the authors highlight that there are two schools of thought in relation to overboardedness. The 'experience hypothesis' proposes that multiple directorships results in invaluable experience and access to vast social networks and resources. On the other hand, proponent of the 'business hypothesis' argue that directors will be unable to properly fulfil their functions if they serve on too many boards simultaneously.

⁹⁵ Rita Esen 'Chartered director qualification: professionalism on UK Boards' (2000) 21(9) *Co Law* 287; 288. And see: Jeremy C Kress 'Board to Death: How Busy Directors Could Cause the Next Financial Crisis' (2018) 59(3) *Boston College L Rev* 877.

⁹⁶ See in general in this regard: Ringe 'Beyond "Independent" Directors' (n3) 1553.

instruments, it is surprising that the exact significance and precise meaning of ‘independence’ has been given so little theoretical consideration.⁹⁷

Independence is of course, no more than a means to an end, constructed to achieve a particular purpose. It may be implemented to counter the classic agency conflict between managers and a dispersed shareholder body.⁹⁸ If this is the case, independence from management and specifically the influential CEO ‘of the stereotypical US Berle-Means corporation’ is probably the dominant criterion. If, on the other hand, independence is aimed at protecting minority shareholders from potential abuses being perpetrated by controlling block shareholders (as is more common in typical Continental European or many Asian companies) independence from the dominant shareholder is by far the most important concern.⁹⁹ As such, different jurisdictions define (or at least attempt to define) independence to reflect the realities of their context. There are commonalities, such as the fact that the independent director must usually be non-executive (ie. not part of the company’s management team).¹⁰⁰

Like definitions related to the term, the role of the independent non-executive is unclear in many jurisdictions.¹⁰¹ The UK Corporate Governance Code 2018 expects non-executive directors to provide ‘constructive challenge, strategic guidance, offer specialist advice and hold management to account.’¹⁰² It also envisages a ‘prime role’ for non-executive directors in appointing and removing executive directors.’ In particular, non-executive directors should ‘scrutinise and hold to account the performance of

⁹⁷ Baum (n14) 5.

⁹⁸ See further on the ‘agency dilemma’ chapter 6 at text to note 92.

⁹⁹ Baum (n14) 4. And see: Harvey Gelb ‘Corporate Governance and the Independence Myth’ (2006) 6 *Wyo. L. Rev.* 129 where the author laments the inconsistent approach to personal and professional ties that might radically undermine independence.

¹⁰⁰ Baum (n14) 5.

¹⁰¹ Le Mire (n6) 6.

¹⁰² UK Corporate Governance Code: Principle H.

management and individual directors against agreed performance objectives.¹⁰³

There are tensions inherent to the role as it is carved out by the code but the constraints that potentially prevent the independent non-executive director from fulfilling his functions optimally are as old as the office itself.¹⁰⁴ Chief among these are constraints of time and information. At a time when countries like the United Kingdom were only starting to opt into a system reliant on the independent non-executive director, it was already apparent to many that, given the time allowed for meetings and preparation it was ‘clearly impossible to expect the board, whatever the law may say to “manage a corporation”’.¹⁰⁵

In fact it is partly this state of affairs that inspired Eisenberg’s emphasis on the monitoring function of the board; the argument that companies had become too big and too intricate to be managed by persons committing only a few working days a year.¹⁰⁶ He concluded that this ‘precludes the board from making business policy: In a complex organisation, concerned with

¹⁰³ UK Corporate Governance Code: Provision 13. See also Le Mire (n6) 7: where the author argues in favour of a role defined by four main aspects, namely the non-executive as a monitor, strategist, resource-gatherer and colleague. Yet even in an explanation of what each aspect entails the inherent tensions remain undeniable. It is practically difficult to be a monitor and a colleague, for example.

¹⁰⁴ See for example a comprehensive analysis by Brudney (n12) 597. And see: Elke Hellinx ‘Steeplechase in the boardroom: the obstacles for non-executive directors to fulfil their role in public companies’ (2017) 38(1) *Co Law* 15; Sarah Kiarie ‘Non-executive directors in UK listed companies: are they effective?’ (2007) 18(1) *ICCLR* 17; Roberta Karmel, ‘Is the Independent Director Model Broken?’ (2013–14) 37 *Seattle Law Review* 775.

¹⁰⁵ Boyle (n1) 491. And see: Ran Duchin, John G Matsusaka & Oguzhan Ozbas ‘When are outside directors effective?’ (2010) 96 *JFE* 195 where the findings support the conclusion that the effectiveness of the outside director depends on the cost of acquiring information about the firm, with outside directors being most effective where information cost is low.

¹⁰⁶ Esen relates the following remark by a US SEC Chairman which captures the sentiment: ‘I don’t care how talented you are, you can’t be a good watchdog if you’re only on patrol three times a year.’ Esen (n66) 205.

complex choices, policy cannot be developed on a part-time basis.’¹⁰⁷ A further constraint was the fact that management tended to provide independent non-executives with inadequate information, added to the fact that they tended not to have their own resources and staff, or separate access to company auditors and related information. And such control over the information presented, was really tantamount to power over the decision itself.¹⁰⁸ In other words, the fact that the director is independent, paradoxically left him/her to rely on information provided by or at least under the direction of management. The paradox is especially evident in the case of super-majority boards in the United States. As independent directors have no direct relationship with the company, an entirely independent board relies heavily on guidance and information curated by the CEO - with the ironic result that ‘independency creates dependency’.¹⁰⁹ Following the Higgs report, Nolan also argued that independent non-executive directors should be given the more focussed task of monitoring management in general and controlling the executive directors’ conflicts of interest in particular, and that they should not continue to have any noteworthy management functions in addition.¹¹⁰

A further challenge was the fact that independent directors tended to be somehow linked to the company’s chief executive and often had an interest in maintaining his goodwill.¹¹¹ This often remains the case, and as South African author Ramani Naidoo pointed out, non-executive directors are still

¹⁰⁷ Melvin A Eisenberg ‘Legal Models of Management Structure in the Modern Corporation’ (1975) 63 *California Law Review* 379. And see: Brudney (n12) 612; Esen (n66) 205.

¹⁰⁸ Boyle (n1) 492. And see: Reggy Hooghiemstra & Jaap van Manen ‘The Independence Paradox: (im)possibilities facing non-executive directors in The Netherlands’ (2004) 12(3) *Corporate Governance: An International Review* 314.

¹⁰⁹ Baum (n14) 17 emphases added.

¹¹⁰ Richard C Nolan ‘The Legal Control of Directors’ Conflicts of Interest in the United Kingdom: Non-Executive Directors Following the Higgs Report’ (2005) 6 *Theoretical Inquiries in Law* 413, 414.

¹¹¹ Esen (n66) 205.

rarely picked for their ability to challenge management; '[o]n the contrary, they are more often chosen for their business, personal or political ties, or for their ability to add symbolic lustre to a company's board. Since they are selected by management, paid by management and, most importantly, informed by management, it is relatively easy for directors to become captive to management's point of view.'¹¹²

Following the financial crisis, the Walker report highlighted failings such as a lack of basic insight and understanding of the businesses whose affairs the independent directors were overseeing – perhaps an even deeper concern in the context of banks and other financial services providers with complex and volatile schemes and products.¹¹³ The time it would take to truly grasp these matters may well require such a commitment from the non-executive director that his/her independence could be undermined. These are not the only conflicts inherent to the position. For example, an effective relationship between the executives and the independent non-executives is premised on some level of trust which is undermined by the fact that the independent non-executive is required to act as 'whistle-blower'.¹¹⁴

¹¹² Ramani Naidoo *Corporate Governance: An Essential Guide for South African Companies* (Juta 2002) 105. And see: Esen (n66) 205.

¹¹³ David Walker *A review of corporate governance in UK banks and other financial industry entities: Final recommendations* (2009) available online at https://webarchive.nationalarchives.gov.uk/+/www.hm-treasury.gov.uk/d/walker_review_261109.pdf at page 43. In fact, these concerns were raised by others in relation to the banking sector specifically some time before the financial crisis hit. See for example: Adrian Buckley and Mattheus van der Nat 'Derivatives and the Non-executive Director' (2003) 21(3) *Eur.n Manag. J* 389.

¹¹⁴ Sweeney-Baird (n12) 71. And see for example on the so-called 'structural bias' that arises when directors in the American context are called upon to determine whether derivative suits against colleagues should proceed: Kenneth B Davis Jr 'Structural Bias, Special Litigation Committees and the Vagaries of Director Independence' (2005) 90 *Iowa Law Review* 1305. See also: Hellinx (n104) 17 where the author highlights contradictions in the core functions of the independent non-executive director. However, cf Leech and Mundheim (n56) 1805, where the authors pointed out that the monitoring role does not imply that the non-executive director should substitute their own judgement for that of management, but also

Despite these paradoxes, the independent non-executive's role is 'most often *assumed* to be monolithic, fixed and even universal'. There is an assumption that an increase in independent directors obviously improves corporate governance although the manner of these improvements is rarely considered. Accepting all this, on what appears to be blind faith alone, has often resulted in the discussion surrounding the independent director being reduced to 'a myopic consideration of the appropriate proportion of independent directors that should be on boards'.¹¹⁵

Those most cynical might even argue that the independent non-executive director was never anything more than a shield, allowing company managers to escape liability and that it did not change the grass roots reality that management was calling the shots. Critics have argued that modern board structures, dominated by the monitoring board, is nothing more than a smoke screen, or façade of corporate governance which creates a dangerous and false sense of security.¹¹⁶ Boards with managerial powers held at least the advantage that the centre of corporate power was clear and you could know the proverbial enemy.

Despite such doom and gloom, some remain more positive about the role of the independent non-executive, and contend that expertise can be a useful partner to independence,¹¹⁷ and that the solution lies in a more practical analysis of board dynamics – with the most successful boards being those

crucially, that the monitoring role does not necessarily imply and adversary attitude toward management.

¹¹⁵ Baum (n14) 6. Most studies on the impact of the independent non-executive on performance find only 'small, statistically insignificant correlations' see: Duchin and others (n105) 196. However, cf Pornsit Jiraport at al 'How do independent directors view powerful CEO's? Evidence from a quasi-natural experiment' (2016) 16 *Fin. R. L.* 268.

¹¹⁶ LE Mitchell, 'The Trouble with Boards', in F. C. Kieff and T. A. Paredes (eds.), *Perspectives on Corporate Governance* (Cambridge UP 2010) 17.

¹¹⁷ Le Mire (n6) 1. The author makes a clear case that the regulatory focus on expertise 'lacks sophistication and coherence' and identifies three particular strands of expertise that are relevant in the context of the company board.

where directors work together in a collegial but rigorous manner. They argue that the various roles of the independent non-executive should compliment each other and should not be seen as inherently contradictory.¹¹⁸ It is also telling that, despite the many criticisms, the drafters of the UK Corporate Governance Code have not chosen to jettison the independent non-executive as a foundational concept but have instead chosen to refine the role slightly, with added emphasis on skills and the fact that independence should not undermine the fact that the board should be fit for purpose.¹¹⁹

The UK Code speaks directly to some of the concerns raised above.¹²⁰ It requires that the board should 'include an appropriate combination of executive and non-executive (and in particular, independent non-executive) directors, such that no one individual or small group of individuals dominates the board's decision-making.'¹²¹ Although there is no limit imposed on the number of boards any one director may sit on, the principles do insist that non-executive directors should have sufficient time to meet their responsibilities.¹²²

In summation, independence often comes at a cost. Most notably, a certain lack of credibility as one must question internal processes from the position of outsider.¹²³ Matters are complicated further by the fact that the knowledge of the company, and entrenchment in its processes that may be required to challenge these perceptions will often negate the sought after independence.

¹¹⁸ John Roberts, Terry McNulty and Philip Stiles, 'Beyond Agency Conceptions of the Work of the Non-Executive Director: Creating Accountability in the Boardroom' (2005) 16 *Br. J. Manag* S5, S6.

¹¹⁹ Hannigan (n52) 363.

¹²⁰ Many of the issues were also dealt with in previous iterations of the Code in response to the reviews prompted by the 2007/2008 financial crisis. For an overview of these developments see: Hannigan (n52) 364.

¹²¹ UK Corporate Governance Code: Principle G.

¹²² UK Corporate Governance Code: Principle G.

¹²³ Esen (n66) 205; Ian GC Stratton 'Non-executive directors: are they superfluous?' (1996) 17(6) *Co Law* 162.

As long ago as 1976 Leech and Mundheim lamented the fact that the CEO regarded the board as ‘his board’: members were selected (in fact though not in law) because they would not rock the boat, information was carefully curated and agendas were set to be as uncontroversial as possible. At the time the authors remained hopeful that these practices and attitudes could change but warned that it would not be enough to encourage the chief executive to ‘want to have a board which does an effective monitoring job’.¹²⁴ Instead, they emphasised that ‘the only effective instrument for change is the *institutionalization of processes that make it mandatory* for the chief executive to account to a strong board’.¹²⁵ The authors at the time made the crucial point that ‘[a]s a practical matter, these responsibilities can only be fulfilled if accountability rests on *institutional procedures* rather than on the willingness of an outside director individually to take unpleasant initiatives at board meetings or otherwise appear to be acting in a personally hostile manner.’¹²⁶

It would again appear that the more things change, the more they stay the same. Following the financial crisis and the volumes of research that it sparked, it is surprising how these observations remain as relevant as they had been some 40 years ago.¹²⁷ And it is arguably exactly in this regard that the corporate governance codes have a more pronounced role to play. Much of the codes have in mind exactly the institutionalised mechanisms that would ensure that the independent non-executive is able to properly function in the complex role that is ascribed to him. The challenge remains the fact that in many instances executives and management are loath to

¹²⁴ Leech and Mundheim (n56) 1826. And see: Boyle (n1) 492 where the author echoes these sentiments.

¹²⁵ Leech and Mundheim (n56) 1826 (emphasis added).

¹²⁶ Leech and Mundheim (n56) 1826. Though they do also contend that the non-executive should himself insist on the processes being put in place in an acknowledgement of the new dimensions of his/her role.

¹²⁷ It bears mention that the emphasis was on the role of the non-executive in representing the interests of the shareholders as his main constituency and as such it does not hold sway in the context of the United Kingdom and modern approaches to the director’s role without some qualification.

institutionalise a process that would see them face actual and dynamic monitoring by a strong board and especially by objective, well-informed and skilled non-executive directors. As long as it is possible for the very mechanism aimed at ensuring efficient functioning of the role to be scoffed of as a box-ticking exercise it remains doubtful whether the independent non-executive will truly be able to live up to expectations.

5 Conclusion

It has been said that 'there are no 'mysteries in the work of the board that require a particularly 'professional' approach in its *outside* directors.' No school-or profession-can supply the principal qualities of the effective outside director. The best qualities are 'general business experience, an enquiring and mind and strength of character'.¹²⁸

For skills that can't be taught, those required by the independent non-executive are highly prized and, perhaps understandably, not something one can kick out from behind every bush. This chapter considered the history of the office of the independent non-executive director and highlighted the high premium that the corporate governance community place on it. However, despite the office being such a strong feature of corporate governance codes and a mainstay of company boards worldwide, it is not to say that the independent non-executive is in fact able to safeguard good governance. There is a dearth of empirical support for staffing boards with independent directors which belies the 'faith and fortune internationally placed on board independence as well as the corresponding enthusiasm of policymakers to promote and enforce it.'¹²⁹ It would appear that the continuity of the status quo is based on little more than blind faith and is not anchored in data and rationality.

¹²⁸ Leech and Mundheim (n56) 1811.

¹²⁹ Baum (n14) 33.

However, given that a board of directors with at least some form of monitoring functions is as old as the joint stock corporation itself, it could as likely be that ‘the concept of the monitoring board may, like democracy, only be a second best option – but yet better than any alternative.’¹³⁰

The question then becomes, how does one regulate this ‘second best’ option to ensure that it is functioning optimally? One possibility is an (arguably) more onerous approach to the interpretation of directors’ duties, taking cognisance of the emphasis that is placed on the monitoring role that these directors play. In applying and interpreting not only the duties but also the business judgement rule and other ‘safe harbour’ provisions,¹³¹ should the courts in some way bear in mind the requirements of the very codes that have given the independent non-executive director the almost cult-like status that he now enjoys?

It may be that this added emphasis will give independent non-executives pause before accepting appointment and may force them to engage in a meaningful way with both the governance reports and the company’s, managers and executives that they monitor. Might it also serve to empower the non-executive? By ensuring that the governance systems proposed by the voluntary codes, that would entrench the position of a strong and dynamic board are truly embraced, could such an approach perhaps ensure that the voice of the independent non-executive gains greater legitimacy in the boardroom? There are also further concerns. As will be considered and expounded upon in subsequent chapters, a balance must be struck when monitoring company directors. Amongst other things, the efficiencies created by delegation could well be undermined by an inappropriate number of checks and balances being put in place. Add to this, general perceptions regarding company law and the role of the regulator when

¹³⁰ Baum (n14) 33.

¹³¹ See discussion in Chapter 7 below at note 80 onwards.

formulating it, and it becomes clear that it will be no simple task to keep a tighter leash on the watchdog.

The following chapters will consider in greater detail, two pertinent directors' duties – identified in chapter 1, before turning to the constitutional and normative constraints that pertain to their interpretation. Where applicable, further reference will be made to the independent non-executive director, and the matter will be considered in conclusion, in chapter 8.

CHAPTER 3

THE DUTY OF CARE AND SKILL

[T]here is a clear public perception that rogue individuals have managed to get away with the unimaginable, and managed this simply because of the lack of appropriate supervision by their corporate directors and senior managers. The non-lawyer's immediate response is that directors ought to be made liable to the company for such failures. The lawyer is less optimistic: the standard of care required of company directors is widely regarded as so low as to be derisory.¹

1 Introduction and Context

As mentioned briefly in chapter 1, the duty of care and skill is one of the mechanisms of constraint imposed upon company directors to ensure that they manage the affairs of the company with an appropriate degree of attention. The broad question that the research considers is whether it is constitutionally tenable and/or normatively desirable for the courts to consult voluntary codes of governance when interpreting and applying this duty – potentially even to the extent of 'reading in' the former's contents.² The duty of care and skill offers fruitful grounds for consideration. Traditionally, it has been confined to a dusty corner and rarely used.³

¹ Sarah Worthington, 'The Duty to Monitor: A Modern View of the Director's Duty of Care' in F Patfield F (ed), *Perspectives on Company Law: 2* (Kluwer Law International 1997) 181.

² The term is used informally here to denote an interpretation which would consider the principles contained in the Code to comprehensively inform the duty (both in common law and the codified version thereof).

³ Worthington, 'The Duty to Monitor' (n1) 181 where the author notes that '[h]istorically, all has hung on directors' fiduciary duties'. See in the context of South Africa also: Natasha Bouwman 'An appraisal of the modification of the director's duty of care and skill' (2009) *SA Merc LJ* 509, 526. Currently it is only in the case of *Niagara (in liquidation) v Langerman & Others* 1913 WLD 188 that directors have been held liable for a breach of the duty of care and skill. This is also the case in many other European jurisdictions, see: Carsten Gerner-Beuerle and

Despite this it provides an interesting ‘case study’ for the potential impact of the corporate governance code. On the one hand, it allows one to consider whether the importation of governance norms might serve to invigorate and redefine the duty itself. On the other hand, it allows one to speculate on the exact practical impact that such an approach to interpretation might have.

To this end the following analysis will investigate the roots and development of the duty of care and skill and identify how this duty has been moulded over time. If one aims to consider the role that voluntary governance codes might play in developing the duty in future (and indeed any potential impact that it might have had on its development to date) it is important to understand the underlying philosophy that has driven the judiciary to develop the duty in the manner that it has done.

The analysis of this chapter will focus on the substance and application of the duty of care as such. It will become clear that its exact scope and contents remain uncertain and somewhat fluid, in both the South African and English legal contexts.⁴ It is also apparent that the courts have adapted their interpretation of the duty to better accord with prevailing societal attitudes and expectations. This is significant as far as the central question of this thesis is concerned as it would, at least at first glance, appear as

Edmund-Philipp Schuster ‘The evolving structure of directors’ duties in Europe’ (2014) 15(2) *EBOR* 191, 199.

⁴ This area of the law has generated significant debate and commentary. Leading texts and comments include: Paul L Davies & Sarah Worthington *Gower’s Principles of Modern Company Law* (Sweet & Maxwell 2016 10th ed) 478; Keay A *Directors’ Duties* (Jordan 2009) chapter 8 at 173; Simon Mortimore (ed) *Company Directors – Duties, Liabilities, and Remedies* (Oxford 2017 3rd Ed) 328; Brenda Hannigan, *Company Law* (4th edn, Oxford 2016) 236; Joan Loughrey (ed) *Directors’ Duties and Shareholder Litigation in the Wake of the Financial Crisis* (Edward Elgar 2013); A Walters ‘Directors’ Duties: the impact of the Company Directors Disqualification Act 1986’ (2000) 21(4) *Co Law* 110; C A Riley ‘The Company Director’s Duty of Care and Skill: The Case for an Onerous but Subjective Standard’ (1999) 26(5) *MLR* 697; Vanessa Finch ‘Company Directors: Who Cares About Skill and Care?’ (1999) 55(2) *MLR* 179; Susan Watson & Andrew Willekes ‘Economic loss and directors’ negligence’ (2001) *JBL* 217.

though the duty of care and skill remains ripe for further development.⁵ If this is accepted, the question this research seeks to answer is whether the more detailed and (potentially) more onerous standards propagated by the governance codes are perhaps the next step, particularly as far as independent non-executive directors are concerned. At its core, the question relates to the standard of care and how this is to be determined.

An approach that favours an outright objective standard, for example, is arguably more suited towards an interpretation that takes into account the principles espoused by the self-regulatory codes.⁶ Pinning down a particular standard also raises the ubiquitous question of whether the duty should be merely a so-called 'norm reflecting' duty or whether it should, to the contrary, be a so-called 'norm setting' duty?⁷ In this regard, Loughrey suggests that a more objective standard indicates that the duty is norm-setting, but points out that the courts may nevertheless remain reluctant to find directors liable for conduct that fails to conform to existing market norms. The author observes that a standard of care set at a level that is higher 'than that adopted by the market at the relevant time may be viewed as too onerous, and as creating the risk that people may be deterred from taking up directorial positions or from engaging in risky behaviour that drives entrepreneurial behaviour and the economy'.⁸

What Loughrey captures are the critical balancing acts to which developments such as the so-called 'business judgement rule'⁹ also speak: how to regulate and curb the power of company directors and establish

⁵ Most commentators who have considered the duty of care and skill (or the duty of care, skill, and diligence as it is now) have concluded unanimously that it requires some reform. See discussion below at text to note 107 – note 135 and sources cited.

⁶ See however below the approach suggested by Riley and comments at text to note 112.

⁷ Loughrey (ed) (n4) 39. And see: Bryan Clark 'The director's duty of skill and care: subjective, objective or both?' (1999) 27 *Scots Law Times* 239.

⁸ Loughrey (ed) (n4) 39.

⁹ See further the discussion on the 'business judgement rule' in chapter 7 at 203.

accountability on the one hand, without stifling robust and forward-thinking management on the other.

Given the impact of English law on especially this part of South African company law, the development of the duty of care and skill will be discussed with reference to both South African and English precedent. Recent developments in both jurisdictions have resulted in some divergence, which the second part of this chapter will highlight and consider.¹⁰ Finally, an overview of the debates and criticisms surrounding the duty of care and skill is provided, and some reference made to the potential practical impact of the provisions of King IV.

2 History and Early Development

The earliest decisions concerned with breaches of the duty of care and skill in English law, show an ‘undemanding’ standard.¹¹ In fact, these judgements will appear quite startling to the modern legal scholar.¹² There are several examples that illustrate how famously low the courts set the bar.¹³ So, a director escaped liability based on the fact that he was ‘a country gentleman and not a skilled accountant’.¹⁴ Ignorance proved an effective defence also to the Marquis of Bute (who inherited the directorship from his father at the tender age of six months),¹⁵ and the directors of a rubber company who

¹⁰ Most notably, the Company Directors Disqualification Act 1986 and the Companies Act 2006 in the United Kingdom and the Companies Act 71 of 2008 in South Africa.

¹¹ Keay *Directors’ Duties* (n4) 182. And see: Blanaid Clarke ‘Duty of care, skill and diligence – from warm baths to hot water’ (2016) 56 *Irish Jurist* 139,152; Clark (n7) 239.

¹² Walters (n4) 111. See also Loughrey (ed) (n4) 12.

¹³ Historically, a plaintiff would have to prove ‘gross’ negligence to hold a director liable. See for example: *Giblin v Mc Mullen* (1868) 2 LR 2 PC 317; *Overend & Gurney Co v Gibb* (1872) LR 5 HL 480; *Lagunas Nitrate Co v Lagunas Syndicate* [1899] 2 Ch 392. See also: Mortimore (ed) (n4) 328.

¹⁴ *Re Denham & Co.* (1883) 25 Ch.D. 752.

¹⁵ *Re Cardiff Savings Bank* [1892] 2 Ch. 101.

could undertake to manage the corporation 'in complete ignorance of everything connected with rubber, without incurring responsibility for the mistakes which may result from such ignorance.'¹⁶

These decisions, however, would not have confounded the man on the street as they merely reflected the cultural conceptions of the time.¹⁷ In reference to *Brazilian Rubber Plantations* Lord Hoffman noted that no-one would have expected the directors to have troubled themselves with the viability of a rubber business as such technical matters were not their concern. 'They were fund-raisers, lending their names, titles and respectability in inviting the public to subscribe for shares. And sophisticated Edwardian investors would have had no illusion about how much or how little this meant.'¹⁸ This view reiterates that the courts considered directors essentially as amateurs involved only intermittently.¹⁹ What is more, at a time when the company was conceptually still closely associated with its shareholders (even as far as the judiciary was concerned),²⁰ the courts took the position in many cases that the shareholders had only themselves to blame if they chose to appoint incompetent or inept directors.²¹

Keay pointed out that the courts in the nineteenth and early twentieth centuries treated issues of care, skill and diligence by asking whether the director was acting in good faith when he made a relevant decision or took a particular action.²² Thus, matters were considered from a good faith perspective as opposed to one that took into account competence or

¹⁶ *Re Brazilian Rubber Plantations and Estates Ltd* [1911] 1 Ch. 425.

¹⁷ Walters (n4)112.

¹⁸ Lord Hoffmann's lecture on Lord Hoffmann 'The Company Director Today' given 26 November 1996 at the Fourth Annual Leonard Sainer Lecture (1997) 18(7) *Co Law* 195.

¹⁹ See for example *Re Denham & Co* (1883) 25 ChD 752 . See also: Keay *Directors' Duties* (n4) 179.

²⁰ Keay *Directors' Duties* (n4) 179.

²¹ See for example: *Turquand v Marshall* (1869) 4 Ch App 376; *Overend & Gurney & Co v Gurney* (1872) LR 5 HL 480.

²² Keay *Directors' Duties* (n4) 179.

diligence. In instances where liability was incurred, the facts constituted a very clear breach.²³ Directors were treated as ‘trustees’ or ‘quasi-trustees’ and therefore the duties formulated by the courts ‘were not based on any benchmark of professionalism nor did they heed the many differences in law and practice that distinguish directors and trustees.’²⁴

The cases mentioned above, and others, culminated in the seminal decision of *In re City Equitable Fire Insurance Co.*²⁵ In his judgement, Romer J formulated three propositions that would dominate this branch of company law for almost the remainder of the century:

(1) A director need not exhibit greater skill than can be expected of a person of his or her knowledge and experience. (2) A director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodical board meetings, and at meetings of any committee of the board upon which he happens to be placed. He is not, however bound to attend all such meetings, though he ought to attend whenever, in the circumstances, he is reasonably able to do so. (3) In respect of all duties that, having regard to the exigencies of business, and the articles of association, may properly be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly.²⁶

Romer J thus endorsed the approach of Lord Hatherley L.C. in *Overend & Gurney & Co v Gurney*,²⁷ namely that the care that directors must take should be measured against the care that an ordinary person could be

²³ See for example *Gould v Mt Oxide Mines Ltd (in liq)* (1916) 22 CLR 490. See also: Keay *Directors’ Duties* (n4) 179.

²⁴ Finch (n4) 200.

²⁵ 1925 Ch 407 at 427.

²⁶ 1925 Ch 407 at 428-429.

²⁷ (1872) LR 5 HL 480. Indeed it was also in this judgement (*Overend & Gurney & Co v Gurney*) that Lord Hatherley L.C and Lord Chelmsford concluded that directors would be liable only in instances of gross negligence (*crassa negligentia*) at 487, 488, 489.

expected to take when managing his or her own affairs.²⁸ It would appear then as though '[t]he director is obliged only to do as much as could be expected from someone as incompetent and foolish as he happens to be ...'²⁹ Or, as Ferran explained in turn '[t]he problem with a duty formulated as in the *Re City Equitable* decision ... is simple and obvious: incompetence is its own defence.'³⁰

In spite of this apparent degree of subjectivity, it is probably not correct to consider the court's approach in *City Equitable* void of all objectivity.³¹ In this regard it has been argued that the test was basically objective, considering that the courts have to ask whether or not the directors 'exceeded the powers entrusted to them, or whether if they did not so exceed their powers they were cognisant of circumstances of such a character, so plain, so manifest, and so simple of appreciation, that no men with any ordinary degree of prudence, acting on their own behalf, would have entered into such a transaction as they entered into?'³² The comparison is thus with a 'man with any ordinary degree of prudence', and, at least to that extent, objective.³³

Regardless of one's take on the case, there is no denying that *City Equitable* made its influence felt not only in England, but also in other Commonwealth jurisdictions. It was heavily relied upon by Morgan J when deciding the first landmark case in South African law - *Fisheries Development Corporation of SA Ltd v Jorgensen and Another*.³⁴

²⁸ *In re City Equitable Fire Insurance Co.* 1925 Ch 407 at 427 – 428.

²⁹ Mackenzie, 'A Company Director's Obligations of Care and Skill' [1982] *JBL* 461.

³⁰ Ferran *Company Law and Corporate Finance* (Oxford UP 1999) 213.

³¹ A Hicks 'Directors' Liabilities for Management Errors' (1994) 110 *LQR* 390; Keay *Directors' Duties* (n4) 181.

³² (1872) L.R. 5 H.L. 480 at 487.

³³ See also: Keay *Directors' Duties* (n4) 181.

³⁴ 1980 (4) SA 156 (W). For a general overview of the development of the duty in South African law see also: Mildred Bekink 'An historical overview of the director's duty of care and skill: from the nineteenth century to the Companies Bill of 2007' (2008) *SA Merc LJ* 95; Bouwman (n3) 509.

Morgan J confirmed the established and accepted rule that a company director has a duty of utmost good faith towards the company. Drawing from several English decisions³⁵ Morgan J set out general guidelines or principles which (not unlike *City Equitable*) served to define South African courts' interpretation of the duty of care and skill for years to come. As mentioned in chapter 2 above, the court distinguishes between the executive and non-executive director in its analysis.³⁶

As a general principle, and in reliance on both *City Equitable* and *Brazilian Rubber Plantations* the court confirmed that a director will not be held liable for mere errors in judgement. The court also concluded that it would be sound for a director to rely on reports prepared by others and to delegate duties that may properly be left to another official. In the absence of grounds for suspicion, the director is then justified in trusting that the official in question will perform these delegated duties honestly. It is noteworthy that Morgan J stated expressly that the director 'is entitled to accept and rely on the judgment, information and advice of the management, unless there are proper reasons for querying such.'³⁷ This last statement resembles the so-called 'common law business judgement rule' although, as the discussion of this rule in chapter 7 below will illustrate, this is not necessarily an accurate term to use in this context.³⁸

Naturally, a director may not accept information and advice blindly, but instead must give it due consideration and must still exercise his/her own judgement. A director may not be a mere dummy, nor may he/she shelter behind what the court terms 'culpable ignorance or failure to understand

³⁵ See *Fisheries Development Corporation v Jorgensen* (ibid) at page 166 where the court relied on (inter alia): *Lagunas Nitrate Co v Lagunas Nitrate Syndicate* (1899) 2 Ch 392; *In re Brazilian Rubber Plantations and Estates Ltd* (1911) 1 Ch 425; *Dovey v Cory* 1901 AC 477; *In re National Bank of Wales Ltd* (1899) 2 Ch 629; *Huckerby v Elliot* (1970) 1 All ER 189.

³⁶ At page 165 par [H]. And see chapter 2 at text to note 85 - 95 above.

³⁷ At page 166 par [B] – [C].

³⁸ See chapter 7 at text to note 95.

the company's affairs'.³⁹ What exactly would constitute 'culpable ignorance or a failure to understand' was not considered. Culpability may of course refer to some form of intent being required, and given the context of the cases and the whole of the judgement the degree of negligence required to establish culpability would likely be significant.

In the subsequent decision of *Howard v Herrigel*,⁴⁰ Goldstone AJ rejected this approach, reverting to the position that the legal rules that pertain to all directors are the same and that it is not appropriate to draw a distinction between executive and non-executive directors.⁴¹

This may well be true in the nominal sense, but the practical application will of course result in different outcomes. Even Romer J in *City Equitable* emphasised the importance of considering the specific circumstances of each case when applying these generic legal rules.⁴² In this regard he observed as follows:

In order, therefore, to ascertain the duties that a person appointed to the board of an established company undertakes to perform, it is necessary to consider not only the nature of the company's business, but also the manner in which the work of the company is in fact distributed between the directors and the other officials of the company.⁴³

In conclusion, the earliest permutations of the duty of care and skill were undemanding, and the duty was ill-defined. Keay attributes this mainly to the fact that directors were quite clearly being appointed with little to no experience, there were very few decided cases (brought about by the

³⁹ At page 166 par [D] – [E].

⁴⁰ [1991] 2 All SA 113 (A).

⁴¹ At page 131. These observations of the court must prompt one to ask whether this approach is still valid today given the very different roles played by executive and non-executive directors, and indeed the key role played by the independent non-executive director. Debate surrounding the duty of care has given rise to several more nuanced approaches and these are considered further below and throughout the thesis. And see above chapter 2 text to note 85 – 95.

⁴² See also observations below at text to note 48.

⁴³ 1925 Ch 407 at 427.

difficulty of bringing action),⁴⁴ and the courts were reluctant to judge board decisions adversely.⁴⁵ Whether correct or not, the position seemed to be that the tests introduced in *City Equitable* were wholly subjective which in every likelihood further deterred potential actions against directors.⁴⁶

Thus, the earliest history of the duty of care and skill shows a legal rule constrained by the perceptions and societal norms of the time. It was informed by the common practice of directors being appointed for the prestige they could bring to the board. Courts were hindered by the difficulties inherent in more refined definitions. Separate legal personality was a more novel concept, and it is perhaps the case that this also read into less developed approaches to the duty of care and skill that tended to centre around honesty and loyalty while ignoring competence and diligence. One might argue that these early developments hardly remain relevant, as times have changed and (as the discussion below will show) so has the judiciary's stance when it comes to the duty of care and skill.

However, the adage 'the more things change, the more they stay the same' rings true. The executive director of today is usually a highly qualified and experienced (not to mention well compensated) individual. Many of the societal perceptions that served to protect incompetent directors at the turn of the 19th century and beyond clearly no longer apply to executive directors (there are some who would equate executive directors with other

⁴⁴ See also chapter 7 at note 4.

⁴⁵ Keay *Directors' Duties* (n4) 182.

⁴⁶ Keay *Directors' Duties* (n4) 182. See also above at notes 37 and 38. And see: JJ Hanks 'Evaluating Recent State Legislation on Director and Officer Liability Limitation and Indemnification' (1988) 43 *Business Lawyer* 1207, 1232 where the author summarises the prevailing perception: 'Unless they engage in conduct in which no reasonable owner would be likely to engage, directors should not expect to be monetarily liable. No owner is likely to steal from himself – a meaningless act – or intentionally inflict harm on his business – an irrational act. Except for such egregious situations, it is difficult to justify imposing monetary liability on a director for the result of his decisions.'

professionals such as doctors and lawyers).⁴⁷ On the contrary, they are appointed because of their skillset, usually remunerated aggressively, and there is a very clear expectation that they are to devote their skills and time to improve the fortunes of the company they serve. Besides this, their relationship with the company tends mostly to be regulated by contract, with care and skill as an express or implied term, in turn lessening the importance of the statutory or common law duty of care.⁴⁸ In contrast, this is often not the case in the context of the non-executive director. Many non-executive directors are still appointed for the esteem they bring to the board or the value of their connections, and in the South African context, this may relate also to pressures that companies face to transform the face of their boards.⁴⁹ Given this, and the extent to which corporate governance codes rely on the integrity of the office of the independent non-executive director, the application of the duties to these directors are pivotal, and will be the focal point of the research.

⁴⁷ See for example: J Cassidy 'Standards of Conduct and Standards of Review: Divergence of the Duty of Care in the United States and Australia' 2000 (28) *A.B.L.R* 180, 197 – 205; P Redmond 'The Reform of Directors' Duties' (1992) 15 *University of New South Wales Law Journal* 86 113; Angus Young 'Regulating non-executive directors in Australia: a socio-legal approach' (2008) 29(11) *Co Law* 323. Note however that, as Davies and Worthington point out, the imposition of more objective standards against which to measure the duty of care and recent statutory reforms stop short of requiring a directorship to be regarded as a profession. As the authors note further: 'Given the enormous range of types and sizes of companies, it would be odd if all directors were to be regarded as professional.' Davies and Worthington (n294) 480.

⁴⁸ Richard Stevens 'The Legal Nature of the Duty of Care and Skill: Contract or Delict?' 2017(20) *Potchefstroom Electronic Law Journal* 1 at 12. See also: Farouk HI Cassim and others (eds) *Contemporary Company Law* (Juta 2012) 411, 477.

⁴⁹ See for example *Daniels v Anderson* (1995) 16 ACSR 607 664 CA (NSW) at 664: 'Furthermore traditionally non-executive directors have been appointed for perceived commercial advantage such as attracting customers or adding to the prestige and status of the company.'

3 Later and Recent Developments

a. The United Kingdom

The passage of time exposed the shortcomings of the common law, which had remained stagnant.⁵⁰ The first notable departure from the approach taken in *City Equitable* was that of *Dorchester Finance Co Ltd v Stebbing*⁵¹ where company directors were held liable for what the court considered negligent behaviour - the significance was of course a move away from the position established by *Overend & Gurney & Co v Gurney*,⁵² in that gross negligence was not required.⁵³ Following this, further developments were brought about by Lord Hoffman in the decisions of *Norman v Theodore Goddard*⁵⁴ and subsequently *D'Jan of London Ltd Copp v D'Jan*.⁵⁵ These decisions show a response to the apparently incongruous position which saw directors of insolvent companies being measured against what was ostensibly a more onerous and objective standard.⁵⁶ The court applied s 214(4) of the Insolvency Act 1986 (which deals with wrongful trading) beyond the traditional confines of that section in order to formulate a general standard of care and skill expected of directors.⁵⁷

The test denoted a departure from that set out in *City Equitable* by Romer J, in that it introduced an objective standard against which all directors are

⁵⁰ Keay *Directors' Duties* (n4) 182, where the author points out that this was a surprising lack of development, especially considering the emergence of the neighbour principle in the context of the law of negligence.

⁵¹ [1989] BCLC 498.

⁵² (1872) LR 5 HL 480. Indeed it was also in this judgement (*Overend & Gurney & Co v Gurney*) that Lord Hatherley L.C and Lord Chelmsford concluded that directors would be liable only in instances of gross negligence (*crassa negligentia*) at 487, 488, 489.

⁵³ See also: Keay *Directors' Duties* (n4) 182.

⁵⁴ [1991] B.C.L.C 1028 Ch D.

⁵⁵ [1994] 1 BCLC 561.

⁵⁶ Davies and Worthington (n294) 479; Mortimore (ed) (n4) 328.

⁵⁷ See also: *Re Landhurst Leasing Plc, Secretary of State for Trade and Industry v Ball* [1999] 1 BCLC 286 at 344; *Cohen v Selby* [2001] 1 BCLC 176 at [21]. And see also: Hannigan (n4) para 11-2.

measured and drew on a subjective consideration of any one director's abilities where this subjective standard is higher than what is objectively desired. In other words, the subjective limb of the test 'can operate only to increase the level of care required of the director.'⁵⁸ Ironically, it has been argued that the test favoured by Lord Hoffman does not, in fact, bring about as radical a departure from that of Romer J as one might at first believe.⁵⁹ Furthermore, there have been concerns about a test that effectively introduces a higher benchmark for more skilled directors – which is exactly what the revised test does.⁶⁰ Be that as it may, the newly formulated test found favour with various factions⁶¹ and was incorporated into the Companies Act 2006 with minimal changes.⁶² Section 174 of the Companies Act 2006 ('the 2006 Companies Act') now states that:

- (1) A director of a company must exercise reasonable care, skill and diligence.⁶³ (2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with – (a) the general knowledge,

⁵⁸ Davies and Worthington (n294) 479. The authors come to this conclusion because: 'The section attributes to the director the knowledge, skill and experience of *both* the reasonable person and the particular director in question, so the latter is important only when it *adds* to the attributes of the reasonable person.'

⁵⁹ Hicks argued that: 'Romer J was setting out a dual standard, first the minimum and irreducible objective standard of the reasonable care of the ordinary man acting on his own behalf; and secondly, the subjective test that relieves him if he does not have highly specialised expertise. Romer J's subjective test is not intended to reduce the standard of care below that of the reasonable ordinary businessman.' Hicks (n31) 392.

⁶⁰ Finch (n4) 203.

⁶¹ Law Commission - Law Commission, *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties* (Law Comm No 261), 1999, Ch 5. Company Law Review – Company Law Review, *Final Report*, vol 1 (2001), p 346 and Annex C; and see *Developing the Framework* (2000), pp 40-3. Government – *Modernising Company Law* (Cm 5553-I, 2002), paras 3.2 – 3.7. See also: Davies and Worthington (n294) 479.

⁶² Effectively, this development aligned the duty in tort law with the objective, contractual duty. See: Loughrey (ed) (n4) 15.

⁶³ One of the only significant changes is the express inclusion of the word 'diligence' but as Hannigan points out, case law had already concluded that a director was under an obligation to 'exert and apply himself' or face penalties as was the case in (for example) *Re Park House Properties Ltd* [1997] 2 BCLC 530. See: Hannigan (n4) para 11-2, note 9.

skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and
 (b) the general knowledge, skill and experience that the director has.

For some time, valuable guidance on interpreting the duty of care came from the courts in the form of judgements relating to disqualification proceedings brought against directors in terms of s 6 of the Company Director Disqualification Act 1986.⁶⁴ These judgements were important due to the reality that direct action by the company against its directors is seldom taken other than in instances where the company finds itself in insolvent liquidation.⁶⁵

However, there are limits to the usefulness of these decisions. As Loughrey points out, disqualification and care and skill have always been measured by different standards, with the former requiring 'gross negligence' but not the latter.⁶⁶ Furthermore, these decisions have 'dried up' as a source since disqualifications are now predominantly dealt with through administrative undertakings.⁶⁷ (As will become clear, South African law faces the same predicament as far as cases dealing with declarations of delinquency, decided in terms of section 162 of the 2008 Companies Act are concerned).⁶⁸

Of the English disqualification cases, perhaps the most notable was *Secretary of State for Trade and Industry v Baker (No 5) ('Re Barings')*⁶⁹ where Parker J clearly heightens expectations when he concludes that '[d]irectors have, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the

⁶⁴ Hannigan (n4) para 11-3; Loughrey (ed) (n4) 16. And for a general discussion on the impact of the CDDA 1986 see: Walters (n4) 110; Keay *Directors' Duties* (n4) 174.

⁶⁵ Hannigan (n4) para 11-4.

⁶⁶ Loughrey (ed) (n4) 17.

⁶⁷ Hannigan (n4) 11-3.

⁶⁸ See chapter 7 at text to note 43 and par. See in overview: R Cassim 'Delinquent Directors under the Companies Act 71 of 2008: Gihwala v Grancy Property Limited 2016 ZASCA 35' (2016) 19 *PELJ* 1.

⁶⁹ [1999] a BCLC 433.

company's business to enable them properly to discharge their duties as directors.'⁷⁰

Considering these developments, the position now seems to be that a uniform and objective duty of care still applies to both executives and non-executives alike although there will be variations in terms of what the discharge of the duty requires, as the specific functions carried out by any particular director will inform what is expected of him or her.⁷¹

A director may delegate to others, but although an objective standard of care leaves room for such delegation, directors still have to guide and monitor management and so the mere fact that there was appropriate delegation does not imply that the director is allowed to abdicate responsibility and that he/she will have no further duties in regards to the matter.⁷² It has also become clear that, although a negligence suit could be based on instances where the directors acted, and did so with undesirable consequences, almost all cases decided in English law (and as it happens South African law) relates to failures to act or failures to act appropriately.⁷³

The duty of care and skill was always the ugly stepsister to the more robustly enforced fiduciary duties, breaches of which tended to be seen in a more serious light.⁷⁴ All things considered, Davies and Worthington conclude that the codification 'brought the standard of care, skill and diligence required of directors into line with that required generally in other areas of social life by the law of negligence.'⁷⁵ Indeed, together with more recent case law, the approach taken by the British Parliament seemed, possibly, to indicate a

⁷⁰ at 489.

⁷¹ Davies and Worthington (n294) 480.

⁷² Davies and Worthington (n294) 481; Loughrey (ed) (n4) 30.

⁷³ Davies and Worthington (n294) 482, para 16-18.

⁷⁴ Keay *Directors' Duties* (n4) 173. See also Worthington, 'The Duty to Monitor' (n1) 181, where the author points out that losses to the company were historically caused by breaches in fiduciary duties, with losses resulting from negligent behaviour, a more modern phenomenon.

⁷⁵ Davies and Worthington (n294) 483, para 16-19.

shift in attitude and to send a message that breaches of the duties of care would forthwith be taken more seriously.⁷⁶ Whether this indeed materialised remains open for debate, as the discussion below will show.

b. South Africa

The 2008 Companies Act followed the example of its UK counterpart and now includes a codification of directors' duties.⁷⁷ Section 76 applies to all 'directors' as defined in the 2008 Companies Act, but also pulls so-called 'prescribed officers' into its fold along with all members of board committees whether or not they are members of the board itself.⁷⁸ The duty of care and skill as such can be found in section 76(3)(c), which requires a director to 'exercise the powers and perform the functions of director ... 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*' (emphasis added). This is subject to

⁷⁶ Keay *Directors' Duties* (n4) 173.

⁷⁷ See chapter 1 for a discussion of the background to the legislation and the reasons for and merits of the codification of directors' duties. See also chapters 5 and 6 for further comments on the interpretation of the legislation in general and these provisions. See also in general: Jean C Kanamugire & Terence V Chimuka 'The Directors' Duty to Exercise Care and Skill in Contemporary South African Company Law and the Business Judgement Rule' (2014) 5(20) *MJSS* 70; Richard Stevens 'The Legal Nature of the Duty of Care and Skill: Contract or Delict?' 2017(20) *PELJ* 12.

⁷⁸ Section 76(1)(a) & (b). 'Director' is defined in section 1 as "a member of the board of a company, ..., or an alternate director of a company and includes any person occupying the position of a director or alternate director, by whatever name designated." Regulation 38 in turn defines a 'prescribed officer' as follows: "Despite not being a director of a particular company, a person is a "prescribed officer" of the company for all purposes of the Act if that person – (a) exercises executive control over and management of the whole, or a significant portion, of the business and activities of the company; or (b) regularly participates to a material degree in the exercise of general executive control over and management of the whole, or a significant portion of the business and activities of the company."

subsections 76(4) and 76(5) which seem to embody some form of business judgement rule – the exact impact of which is not yet settled.⁷⁹

Section 76 must also be read with section 77 which deals with the liability of directors.⁸⁰ The latter section states that:

A director of a company may be held liable—

- (a) in accordance with the principles of the common law relating to breach of a fiduciary duty, for any loss, damages or costs sustained by the company as a consequence of any breach by the director of a duty contemplated in section 75, 76(2) or 76(3)(a) or (b); or
- (b) in accordance with the principles of the common law relating to delict for any loss, damages or costs sustained by the company as a consequence of any breach by the director of—
 - (i) a duty contemplated in section 76(3)(c);
 - (ii) any provision of this Act not otherwise mentioned in this section; or
 - (iii) any provision of the company's Memorandum of Incorporation."⁸¹

As is the case with section 178(2) of the 2006 Companies Act, the South African duty contained in section 76 can be broken up into three elements. The elements will often overlap, but it is useful to think of them as proposed by Arnold who suggests (as far as the 2006 Companies Act is concerned) that 'care is to be understood as carefulness, though not caution; skill denotes ability, while diligence may be understood as requiring the director to apply himself conscientiously to the affairs of the company and, in particular, the matter at hand.'⁸²

⁷⁹ See below at chapter 5 for a discussion of the impact and contents of these sections.

⁸⁰ It is not yet entirely clear how the statutory provisions might impact the legal nature of the duty. In this regard see: Stevens (n77) 12.

⁸¹ Section 77(2)(a)-(c).

⁸² Mortimore (ed) (n4) 330.

The courts have not yet had the opportunity to state conclusively how the test in section 76 is to be interpreted and applied. The wording does not state expressly that the second leg of the test (the subjective component) could serve only to heighten the standard against which the director is measured but never lower it. However, given the marked similarities between the wording of the 2008 Act and the 2006 Act there is every likelihood that the provision would be interpreted to align with the position in the UK, and in other words, that the subjective element could never allow a director to escape liability where his/her conduct falls below the bar objectively set. In comparing the wording of the South African provision with Australian law, Du Plessis concluded that South African law will now judge liability against the standards of the 'reasonable person' and that as such, the test is objective but with justifiable subjective components given especially the unique emphasis in South Africa on encouraging entrepreneurs to become directors of local companies.⁸³

Finally, despite the significant influence of English law, it must not be forgotten that the duty in South African law remains rooted in delict and that the South African common law duty of care and skill remains 'at heart more subjective than objective – the individual director is considered, and is neither measured against the reasonable person nor against the reasonable director, but what the reasonable thing would have been for *such a director* to have done.'⁸⁴ Despite Du Plessis' faith in the newly introduced standard, Stevens and De Beer argue convincingly that the standard of care may well be reduced to gross negligence, depending on how the courts interpret and

⁸³ Jean J du Plessis 'A comparative analysis of directors' duty of care, skill and diligence in South Africa and Australia' (2010) *AJ* 263.

⁸⁴ Richard Stevens & Philip de Beer 'The duty of care and skill, and reckless trading: Remedies in flux?' (2016) *SA Merc LJ* 250, 253 where the authors also point out that the subjective component of the test is likely 'as much a function of its mixed legal heritage as it is a function of the variable nature of directorship itself.

apply the newly introduced business judgement rule, contained in section 76(4) of Act.⁸⁵

As is the case in the United Kingdom, there is a dearth of actions based on a breach of the duty of care and skill in South African law.⁸⁶ Some decisions offer insights into what is considered “reckless conduct” as the 1973 Companies Act imposed personal liability where companies were managed in a way that amounted to reckless conduct. Proceedings under section 424 of the 1973 Companies Act (and, since 2011, under section 22 of the 2008 Companies Act, which contains similar sanctions) were brought far more regularly as creditors attempted to recoup losses especially where the companies that they contracted with faced liquidation.

Declarations of delinquency as a remedy against errant directors is new to South African law and was introduced by section 162 of the 2008 Act. There have, however, been a number of applications based on the provisions of section 162, and these offer some insight into the meaning of the terms ‘gross negligence’ and ‘wilful misconduct’.⁸⁷ In this regard, Kathree-Setiloane J pointed out that, unlike the concept of a ‘delinquent director’ the former two concepts are not new to South African company law, with gross negligence having been considered in a number of cases.⁸⁸ In this regard the Supreme Court of Appeal noted that gross negligence requires ‘a complete obtuseness of mind’ if the distinction between this type of conduct, and conduct considered merely negligent were to have any remaining

⁸⁵ Stevens & De Beer (n84) 260-261. For a further consideration of this argument and discussion of the business judgement rule in general see chapter 7 at text to note 80 and onwards.

⁸⁶ Bouwman (n293) 526.

⁸⁷ Section 162(5)(c)(iv)(aa) provides that a court must make an order declaring a person to be a delinquent director if the person acted in a manner that amounted to gross negligence, wilful misconduct or breach of trust in relation to the performance of the director's functions within, and duties to, the company.

⁸⁸ *Msimang NO and another v Katuliiba and others* [2013] 1 All SA 580 (GSJ) para [35].

meaning.⁸⁹ Gross negligence, has in turn also been described as connoting 'a particular attitude or state of mind characterised by an entire failure to give consideration to the consequences of one's actions, in other words, an attitude of reckless disregard of such consequences.'⁹⁰

This makes it immediately apparent that, as is the case in the United Kingdom pertaining to matters decided in terms of the Directors Disqualifications Act, decisions on delinquency and disqualification will be of limited use in interpreting the duty of care and skill. Be that as it may, these cases at least point to the type of conduct that would definitely be considered beyond the pale and some of the courts' observations in relation to the interpretation of provisions imposing personal liability or resulting in orders of delinquency remain relevant.

Most recently negligence in the South African context was revisited in *Cape Empowerment Trust Ltd v Druker and others* where Yekiso J makes some interesting remarks relating to the King Code of Governance:⁹¹

I am of the view that the reservations expressed by the applicant, both on the founding and replying papers as well as in its submissions, are justified more particularly when it is glaringly apparent that the King Code of Governance principles relating to compliance with applicable laws and adherence to rules of accepted practice; a duty to ensure the integrity of the companies as vehicles of investment; and the need for the directors to act in the best interest of the company appear not to

⁸⁹ See *Transnet Ltd t/a Portnet v Owners of the MV "Stella Tingas" and another* 2003 (2) SA 473 (SCA) at para 7: ". . . It follows, I think, that to qualify as gross negligence the conduct in question, although falling short of *dolus eventualis*, must involve a departure from the standard of the reasonable person to such an extent that it may properly be categorised as extreme; it must demonstrate, where there is found to be conscious risk taking, a complete obtuseness of mind or, where there is no conscious risk taking, a total failure to take care. If something less were required, the distinction between ordinary and gross negligence would lose its validity."

⁹⁰ *S v Dhlamini* 1988 (2) SA 302 (A) at 308.

⁹¹ [2016] JOL 36987 (WCC).

have been observed, and, as a matter of fact, appear to have been totally disregarded.

The learned judge does not explain the exact role that the King Code plays in her interpretation of the statutory provisions. In fact, it is not entirely clear what the court might be implying with the use of the term 'duty' in the first place. Should it be understood as referring to legal duties, in which case it is not entirely clear what the 'duty to ensure the integrity of the companies as vehicles of investment' could then be. There is no such duty in the 2008 Act, nor was there an independent duty along these lines recognised in South African common law. It is perhaps more likely that the learned judge was speaking more generally and referring, perhaps, to societal norms and expectations. Certainly, Yekiso J seems to consider the principles of the governance code as some form of evidence which informs the duty of care and skill. Although this is not explicitly stated, it appears to inform the objective component of the test, speaking to the behaviour that would generally be expected in practice.⁹²

4 Debate Surrounding the Director's Duty of Care and Skill

a. Practical challenges posed by the duty of care and skill

If ever one were to expect a series of claims against company directors, it would have been in the wake of the 2007/2008 financial crisis. And yet, from Wall Street to the square mile it seemed to have been, just another day at the office.⁹³ Naturally, this might lead to questions surrounding the capacity

⁹² See chapter 5 below for an analysis of the interpretative approach followed by the courts. If, as appears to be the case here, the codes are used as part of the facts presented to establish the objective standard required and thus inform the common law test for care and skill it is submitted that it will likely pass constitutional muster and does indeed fall within the remit of the court.

⁹³ Loughrey (ed) (n4) 7.

of the law to respond. The lack of litigation might speak to obstacles faced by shareholders attempting to hold directors accountable, but might also be since there were in fact no actionable breaches of duty.⁹⁴ This then relates directly to the substance of the duties in general, and in particular the duty of care and skill, and how they are interpreted and applied by the courts.

The consensus following the 2007/2008 financial crisis, was that any blame laid at the door of company directors would have to be based on incompetence. There was little if any evidence of directors lacking integrity or acting dishonestly. As such, claims following the events of 2007/2008 would likely be based on breaches of the duty of care and skill and not breaches of the fiduciary duties.⁹⁵ It is clear that boards would be considered in breach of their duty to monitor if they either completely abdicate it or if they ignore obvious risks and red flags – but only where the response to these risks was equally apparent or obvious, as the case law generally shows a reluctance to hold directors liable for their failure to respond properly to complex situations.⁹⁶

Generally speaking, there are several ‘constraint[s] on judicial enthusiasm for negligence claims’⁹⁷ against directors, that relate also to the fact that there is (in virtually no jurisdiction) a single objective standard of skill. The lack of such an objective standard, and a general reticence on the part of the courts when enforcing the duty have been variously explained. The traditional view,⁹⁸ was that the shareholders have only themselves to blame

⁹⁴ Loughrey (ed) (n4) 8.

⁹⁵ In considering the allegations made against bank directors following the 2007/2008 financial crisis, Loughrey identifies four distinct failures, or sets of conducts, that could potentially have given rise to successful claims against the directors. These are firstly, a failure to monitor or institute risk management systems; second, a failure to keep informed; third, an undue reliance on others or inappropriate delegation practices; and finally, negligent decision making. Loughrey (ed) (n4) 12, 21, 26, 29, 33.

⁹⁶ Loughrey (ed) (n4) 25.

⁹⁷ Hannigan (n4) para 11-5.

⁹⁸ Hannigan (n4) para 11-5; *Blackman’s Commentary on the Companies Act 191* (Issue 7, 2010); Walters (n4) 112.

if they find themselves the victims of an errant director.⁹⁹ As Lord Hatherley LC famously noted, ‘however ridiculous and absurd their conduct might seem, it was the misfortune of the company that they chose such unwise directors’.¹⁰⁰ A shareholder acquires his interest voluntarily, it is argued, and as such it is a simple case of *volenti non fit injuria* and not a matter for the courts.¹⁰¹ However, there may also be another reason for the reluctance shown by the courts and this is based on the general philosophy that defines the approach to company law and regulation, and which is especially prevalent in the United Kingdom (and by extension also became part of the ethos in South Africa). The deference to board decisions may also be reflective of an ingrained perception that company law is inherently a ‘private’ matter and that interference by means of external regulation should be avoided or minimised. This will be considered in greater depth in chapter 6 below.¹⁰²

A second challenge, is the matter of hindsight and the fact that the courts are loathe to substitute their judgement for that of the board, where the

⁹⁹ Hannigan (n4) para 11-5; *Blackman’s Commentary on the Companies Act 191* (Issue 7, 2010); Walters (n4) 112.

¹⁰⁰ *Turquand v Marshall* (1869) LR 4 Ch App 376, 386.

¹⁰¹ *Lagunas Nitrate Co v Lagunas Syndicate* [1899] 2 Ch 392, 426 where Lindley MR notes that ‘[n]o one need join a company unless he likes, and if a person knows that if he becomes a member he will find as directors persons who, in his opinion, ought not to be directors, he should not join the company. If he does he has no right of redress on the ground that improper persons were appointed trustees. *Volenti non fit injuria* applies in such a case to members of the company...’

¹⁰² See for example Moore who considers the ‘fundamental nature’ of the laws relating to the governance in the United Kingdom and points out that in the Anglo-American context corporate law tends to be considered an aspect of private or facilitative law. He contends that ‘judicial deference to internal corporate autonomy likewise persists in the English common law environment under the doctrinal label of the ‘internal management’ doctrine. This rule, together with the comparably longstanding contractual principle that underpins the juridical character of the corporate constitution, has operated so as to affirm the characteristic ‘privity’ of UK corporate law in the sense of its inherently *facilitative* and *non-regulatory* nature.’ Moore *MT Corporate Governance in the Shadow of the State* (Hart 2013) 8.

latter arrived at a decision honestly.¹⁰³ Cases decided in the UK still show the courts' reluctance to basing liability on a director's failure to understand his/her business and what was going on in it. Directors are not required to possess specialist expertise and general knowledge will suffice.¹⁰⁴ The two final concerns centre on the very diverse nature of companies and the directors at their helms. The sheer variety of companies and business endeavours, the myriad different roles that a director or executive might fulfil in the context of each corporation and the fact that directors will come to their office with different backgrounds, training and experience all make a uniform standard an impossibility.¹⁰⁵

In summation, what has traditionally been a dearth of litigation might point to underlying failings as far as the formulation, application and interpretation of the law on directors' duties is concerned. It may also be that, more generally speaking, there is a problem with the 'very concept of shareholders as effective monitors' (an issue that will be dealt with in greater detail in chapter 7 below).¹⁰⁶

b. An overview of the academic debate

The duty of care and skill is certainly embattled. While some have called for it to be jettisoned entirely,¹⁰⁷ others have contended that the duty has a

¹⁰³ *Howard v Herrigel* 1991 (2) SA 660 (A) 676; *Levin v Felt & Tweeds Ltd* 1951 (2) SA 401 (A) 414-415; *Harlowe's Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Co NL* (1967) 121 CLR 483 493 (HC of A); *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821 832; [1974] 1 All ER 1126 1132 (PC).

¹⁰⁴ Loughrey (ed) (n4) 27 – 28.

¹⁰⁵ See for example: *AWA Ltd v Daniels* (1992) 7 ACSR 759 867 SC(NSW); *Daniels v Anderson* (1995) 16 ACSR 607 664 CA(NSW).

¹⁰⁶ Loughrey (ed) (n4) 8.

¹⁰⁷ See for example: Yoram Danziger & Omri Rachum-Twaig 'Re-evaluating the justifications for the existence of an independent duty of care' (2014) 35(9) *Co Law* 265.

continued role to play but that reform is required.¹⁰⁸ Riley argued that it is possible to formulate the duty in a more concrete manner that does not turn on a vague balancing act between risk taking and accountability.¹⁰⁹ He points out that one must differentiate between the *functions* that one wishes the directors to perform, and the *standard* at which one wishes for them to perform those functions.¹¹⁰ The criticisms focus mainly on the fact that the courts have failed to formulate in any meaningful way a clear set of functions or expectations against which the company director's conduct could be measured. However, doing so does not per se imply that one must measure the director against some universal and objective standard. This, he argues, conflates the issues. Once one has homed in on a set of concrete expectations as a starting point, one is then able to measure the conduct of an errant director against this framework in either a subjective or objective manner – depending on which is to be preferred. In other words:

[T]he law can, and certainly ought to, begin by developing an appropriately onerous account of the proper, modern role of directors, including the functions (meaning the tasks and activities) associated with that role. To be sure, such an account would need to be 'tailored' to such individualised factors as the nature of the company which a director serves, the type of director she is, and so on. However, the important point is that the content of this role can be specified independently of the standard of liability by which a director's failure to fulfil its constitutive functions should be judged.¹¹¹

Riley proceeds to propagate a subjective standard, arguing that if it is used in conjunction with properly defined roles and functions, it offers a suitably balanced approach as it would hold the director to clear standards while

¹⁰⁸ Numerous authors have considered the duty over many years and it is not possible to consider all of these viewpoints. The discussion below offers an overview of some of these approaches.

¹⁰⁹ Riley (n4) 699.

¹¹⁰ Riley (n4) 699.

¹¹¹ Riley (n4) 699.

avoiding a scenario where even his or her best attempts at compliance remain sub-par.¹¹²

In turn, Watson and Willekes lament the fact that the courts and scholars have seemingly accepted that directors should not be liable for their own negligence. They describe this as an anomaly in company law, and credit it to a misapplication of the organic theory¹¹³ of company law. The authors propagate a 'more rational' basis, namely the use of assumption of liability. In terms of this approach liability does not hinge on an assessment of the duty of care but is instead determined by considering whether there has been an assumption of legal liability for consequent economic loss by an individual in any given case.¹¹⁴

Finch also argued for a reconfiguring of the duty of care and skill.¹¹⁵ The author called for 'an effective machinery for eliminating directors' incompetence' and pointed out that effective supervision of company directors requires a multi-pronged approach.¹¹⁶ Many have argued that the duty of care and skill is inappropriate or superfluous and should fall away entirely. Certainly, there are many who believe that higher standards would not be effective. As Finch pointed out, even the courts themselves have conceded that '[judges] are not equipped by training or experience to make business judgments because such judgements are intuitively geared to risk taking and often reliant on shifting competition and market criteria.¹¹⁷ On the other hand it has been argued forcefully, that the duty should indeed be more rigorous as a more onerous take on the duty accords with the

¹¹² Riley (n4) 700.

¹¹³ Also called the directing mind theory. See also: R.J. Wickins and C.A. Ong 'Confusion worse confounded: the end of the directing mind theory?' (1997) *JBL* 524.

¹¹⁴ Watson and Willekes (n4) 219.

¹¹⁵ Finch (n4) 201 where the author remarks that: "The common law operates to give directors a remarkable freedom to run companies incompetently. Provided that their behaviour falls short of the grossest negligence they are unlikely to be held to account."

¹¹⁶ Finch (n4) 201.

¹¹⁷ Finch (n4) 202.

responsibilities that are a feature of the office of the modern director, and the law should reflect the higher expectations that society and the business world now have.¹¹⁸

Finch thus argued for an objective test to be applied, but for this test to be defined in such a way that it does not stifle enterprise or discourage directors from improving skill levels. She conceded that a single, objective test does not appear feasible – given that directors do not comprise a homogeneous category. She argued, however, that ‘it does...seem possible to lay down a test that allows judges to consider variations in directorial roles, but which does not ask judges to become involved in the merits of business decisions’ and proposed a formulation that ‘calls on a director to exhibit the skill and care reasonably to be expected of a person who has undertaken their kind of role in their kind of company’.¹¹⁹ This, she argued, would allow the court to consider the size and nature of the enterprise and the skills reasonably associated with the office held by the director in question. Directors are then judged on the functions they undertake with their qualifications not acting as a potential prejudice.¹²⁰

Worthington comprehensively considered the origins of the duty of care and comments specifically on a component of the duty which has become vital given the size and complexity of the modern company: the duty to monitor.¹²¹ She pointed out that many of the famous decisions traditionally seen to support a narrow construction of the duty have actually been misinterpreted or interpreted in a blinkered way and called for the duty to be ‘recognised for what it is’ namely ‘a common law duty in tort to take reasonable care to avoid causing harm to the company’.¹²² As the author

¹¹⁸ Finch (n4) 202. The author also points out that a more onerous standard will reflect a more stakeholder inclusive approach to company law which is coming to the fore.

¹¹⁹ Finch (n4) 202

¹²⁰ Finch (n4) 203.

¹²¹ Worthington, ‘The Duty to Monitor’ (n1) 181. See also in this regard chapter 2.

¹²² Worthington, ‘The Duty to Monitor’ (n1) 201.

pointed out, negligence is a changeable concept as it is inherently dependent on ‘general public sentiment of moral wrongdoing’.¹²³ The analysis concludes with the following pointed observations, which speak to many of the objections that are traditionally raised when a more onerous interpretation of the duty of care is mentioned:

None of this should be seen as putting directors under increased pressure in performing their assigned roles. Delegation, reliance on others, undertaking tasks without any particular professional expertise, and so on, will all remain an acceptable part of the director’s role – but only on the condition that, in the circumstances, they can be seen as a *reasonable* response to the task in hand. The law – even in its modern formulation – is not something to be feared by responsible directors ... none of this does anything more than attach liability where it is warranted, and attach it to the most appropriate party. This should be welcomed: it is one of the important functions of the law.¹²⁴

In making a case for the codification of the duty in South African law, Du Plessis pointed out that ‘there is an inherent difficulty in trying to write bright lines for actions that are judgments taking into account a wide range of facts, circumstances, experiences and expertise.’¹²⁵ Indeed, as the author reminds us, in 200 years the courts have proved unable to do so. However, despite recent legislative intervention (in both the UK and South Africa), the directors’ duty of care, skill and diligence remains opaque. For example, there is no clear indication what a court would consider when determining standards of conduct.¹²⁶ Any inquiry had always required a ‘detailed consideration of all the relevant facts in any particular case’ and this remains

¹²³ Worthington, ‘The Duty to Monitor’ (n1) 202 citing at note 137 the seminal case of *Donoghue v Stevenson* [1932] AC 562, 580.

¹²⁴ Worthington, ‘The Duty to Monitor’ (n1) 202.

¹²⁵ Jean J Du Plessis ‘Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 2’ (2011) 32(12) *Co Law* 377 382

¹²⁶ Loughrey (ed) (n4) 16.

the position.¹²⁷ Matters such as the composition of the board, size and nature of the company and the manner in which functions are distributed are have been identified as examples of relevant concerns when assessing a standard of care.¹²⁸ The level of reward a director is entitled to receive might also be a factor for consideration, with the presumption being that a higher level of reward may reasonably bring about the expectation that greater responsibilities may be implied.¹²⁹

An analysis of the development of the duty shows that one of the matters that has been hindering the courts, has been the difficulties of finding more concrete parameters against which to measure conduct – in drawing the bright lines that Du Plessis speaks of.¹³⁰ It is submitted that the approach propagated by Riley¹³¹ may offer a practical solution and that it is in this context that the principles of the governance codes could provide some useful scaffolding. Riley suggests that the law ought to start off by developing an ‘appropriately onerous account of the proper, modern role of directors, including the functions (meaning the tasks and activities) associated with that role.’¹³² In developing this account, the codes give a concrete overview of what is expected of the company director and provide

¹²⁷ Mortimore (ed) (n4) 332. And see: *In re City Equitable Fire Insurance Co.* 1925 Ch 407 at 427; *Daniels v Anderson* (1995) 16 ACSR 607, 668 cited and adopted by *Jonathan Parker J in Re Barings plc (No5)* [1999] 1 BCLC 433, 488, para B5.

¹²⁸ Keay *Directors’ Duties* (n4) 187. See also for example the remarks made by Lord Hoffman in *Bishopsgate Investment Management Ltd v Maxwell (No 2)* [1994] 1 All ER 261, 264b, CA, which speak to some of the essential issues and summarise in broad terms what might inform the court’s decision: “The law may be evolving in response to changes in public attitudes to corporate governance, as shown by the enactment of the provisions consolidated in the Company Directors Disqualification Act 1986. Even so, the existence of a duty to participate must depend upon how the company’s business is organised and the part which the director could reasonably have been expected to play.”

¹²⁹ *Re Barings plc (No5)* [1999] 1 BCLC 433, para B6.

¹³⁰ Jean J Du Plessis ‘Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 2’ (2011) 32(12) *Co Law* 377 382.

¹³¹ Riley (n4) 697. See analysis at text to note 112. See also further analysis and comments in chapters 5 and 6.

¹³² Riley (n4) 699.

at least some measures that could be valuable in informing the courts' decisions.

In the UK, this would remain limited to listed public entities subject to the provisions of the code. However, in the South African context the drafters of the King Code of Governance have been more ambitious and have insisted since the third version of the Code that its provisions apply to all registered companies in the republic (regardless their size).¹³³ The most recent report contains a number of so-called 'sectoral supplements' and it is possible that these might be a very useful aid in all cases regardless the size of the company or the sector within which it operates. It perhaps represents a first step in developing the very 'account' that Riley speaks of - one which the author concedes would need to be 'tailored to ... individualised factors'.¹³⁴ The approach could prove beneficial to directors in that it would define expectations. A more refined version of the duty may also give the courts the confidence to apply it more robustly in offering more concrete yardsticks or parameters.

An alternative role is that the codes may speak to the matter of 'diligence', the third component of the duties. In this regard the enquiry might simply be: Did the directors truly apply their minds to the code or were they engaged in a box ticking exercise. The latter approach would potentially then speak to a lack of diligence, to the extent that the provisions of the code are aimed at entrenching processes aimed at managing risk and ensuring accountability. This approach might have additional benefits. If one were to consider proper engagement with the codes of governance as a component of the duty of care and skill, it may then serve not only to add depth to the duty of care but also to give additional legitimacy to the governance codes. This stops short of turning the codes into black letter

¹³³ See chapter 1 note 108.

¹³⁴ Riley (n4) 699.

law and retains many of the advantages traditionally associated with a voluntary approach to regulation.¹³⁵

If one considers alternative proposals for the modification of the duty, it is also possible to see how the contents of the codes might play a sensible part. The approach advocated by Finch would see a focus on the kind of role the director plays in the kind of company he is working for. It echoes components of what Riley propagates in that it focusses on functions and expectations – both more readily susceptible to being objectively determined and somehow defined. King IV offers very clear ‘signposts’ from an industry perspective regarding these functions and expectations. It could at least give the courts a base line, or basic presumption that a board that diligently implemented the contents of the code as it applies to the sector concerned had acted in accordance with these objectively determined functions, duties and expectations.

If on the other hand one were to argue, as Worthington does, that liability should be based on a duty of care in tort law it is again conceivable that the content so the governance code could speak to whether ‘reasonable care’ was taken. Although a possible caveat here is again that the argument would not hold if one considers the codes as an indicator of ‘best practice’ as this might allude to a higher standard than what would be required to constitute ‘reasonable care’. That being said, given the complexities of managing a listed company today, it is perhaps not a far-fetched argument that dynamic compliance with the provisions of the governance code should be a point of departure and not some higher aspiration.

¹³⁵ This argument will be considered in greater detail in chapters 7 and 8 below.

5 Conclusion

The preceding analysis has shown that, in the earliest stages of its development, the directors' duty of care, skill and diligence would hardly have cast fear in the heart of the lax or incompetent director. The emphasis was on honesty, loyalty and good faith with little being said about competence - other than that one could not possibly take it for granted that your appointed directors would be at all capable of doing their job. Perceptions have gradually changed and what was initially a dominantly subjective inquiry has become increasingly objective in nature. These developments speak to the fact that societies (and as the 2007/2008 financial crisis made clear) even national economies rely more and more on the fact that the directors that monitor especially bigger companies are competent and diligent when they undertake their tasks.

A number of authors and some judgements by the courts also seem to take for granted that at least some reference will be made to the corporate governance codes.¹³⁶ Yet the cases (and indeed most academics and

¹³⁶ See for example: John Lowry 'The Irreducible Core of the Duty of Care, Skill and Diligence of Company Directors: "Australian Securities and Investments Commission v Healey"' (2012) 75(2) *MLR* 249, 260: 'While the UK Corporate Governance Code lacks the force of legislation, it is likely to be the first port of call for judges when called upon to consider the standard of care of directors in relation to their role in overseeing corporate financial reporting.'; Mortimore (ed) (n4) 77: 'Listed companies are expected to comply with the Combined Code containing principles of good governance and a Code of best practice...This deals with the role of the non-executive directors and indicates what level of commitment is to be expected of them and is likely to be relevant to any issues as to the role and duties of non-executive directors'; Davies & Worthington (n4) 482: 'Although neither the Turnbull Report nor the UK Corporate Governance Code are legislative instruments binding the courts, it is likely that, in appropriate cases, the courts' view of what an objective standard of care requires will be influenced by the provisions. Indeed, that process is already evident in the area of disqualification of directors on grounds of unfitness'; Delpont P & Vorster Q, *Henochsberg on the Companies Act 71 of 2008* (Service Issue 18 LexisNexis 2018) 298(20): 'The various codes that may apply, such as the King IV Code on Corporate Governance, are not law but, it is submitted, do set levels of, at least, the duty of care, skill and diligence' and 'Non-compliance with the requirements of a code, the King IV Code, could under certain circumstances therefore result in liability for breach of that duty'

commentators) that reference the governance codes in the context of the interpretation of the duty of care and skill (and other directors' duties) are vague in defining the exact role that the codes may play in this context and the legal standing that they should be afforded. This chapter has made some suggestions on how the provisions of King IV in particular, but voluntary governance codes more generally, might impact an analysis of the duties. This does not yet address concerns such as the legality of the approach nor does it consider whether such an approach would be normatively sound or sustainable. Before turning to these issues, chapter 4 will consider the fiduciary duty to act in the best interests of the company and how reference to King IV might impact its interpretation and application.

CHAPTER 4

THE DUTY TO ACT IN THE BEST INTERESTS OF THE COMPANY

All systems of governance must seek an appropriate balance between the interests of self and society. That applies to corporate governance just as it does to governance in other areas of society.¹

1 Introduction

As the preceding historical analysis shows, the law has been relatively settled in its approach to the ordinary director as a mandatory who, given his position vis-à-vis the company, was obliged to act in the interests of the latter² and to exercise good faith in doing so.³ This summation is less helpful considering that even the courts have conceded on various occasions that ‘the interests of the company’ remains as unprecise a phrase as any, is at times misunderstood, and may have slightly different meanings depending on the context’.⁴ When we then ask a board of directors to act ‘in the best

¹ Bob Tricker *Corporate Governance: Principles, Policies and Practices* (3rd edn, Oxford, 2015) 71.

² See *Percival v Wright* [1902] 2 Ch 421 Ch D In the context of the United Kingdom this formulation has changed, and the modern codified version of the duty requires the director to promote the success of the company (see below for discussion at text to note 95 and onwards). The statutory version of the duty in South African law continues to refer to the ‘interests’ of the company (see below for discussion at text to note 115 and onwards).

³ In the South African context see: *African Claim & Land Co Ltd v W J Langermann* 1905 TS 494 504 Innes CJ: “An ordinary director is a mandatory, entrusted, in conjunction with his co-directors, with the management of the company's affairs; bound to exercise the utmost good faith in transacting with them; to give the company the benefit of his judgment and experience; and to render that amount of diligence which an ordinary prudent and careful man would display under the circumstances.”

⁴ Nourse LJ made the following telling observation: “[t]he expression ‘the interests of the company’ is one which is often used but rarely defined”, “[i]t seems quite

interests of the company', we may be asking them to align their strategies with any one of a number of interests - interests that may conflict. From this perspective, the central question becomes, whose interests should be on the mind of a company director making a strategic decision? Instead of considering the question from the perspective of the 'interests' of the company or its various stakeholders, one could also choose to frame the debate as a search for an appropriate 'corporate objective'.⁵ In other words, it is only once one has determined what the ultimate goal or purpose of the company should be, that one is then able to consider whether it has fallen short of achieving this goal. If the company fails to achieve its goal, one could argue concomitantly that the correct interests have not been represented or adequately represented. If the goal of the company is, for example, to maximise shareholder value, it will have fallen short of this goal if shareholders fail to enjoy concrete returns.⁶ As such debates about the so-called corporate objective seek to answer the same questions raised by an interpretation and analysis of the phrase 'the best interests of the company' and in turn relates to the extent to which wider interests should potentially be taken into account. For ease of reference this complicated mouth-full will subsequently be referred to as 'the stakeholder debate'⁷.

likely that it is sometimes misunderstood and . . . possibly . . . has slightly different meanings in different contexts' *Brady v Brady* [1988] 2 All ER 617 HL.

⁵ See for example: Anant K Sundaram and Andrew C Inkpen 'The Corporate Objective Revisited' (2004) 15(3) *Organ Sci* 350; Shuangge Wen 'Revisiting the corporate objective through the economic lens – the UK perspective' (2013) 24(8) *ICCLR*302.

⁶ The most famous example of this is perhaps the American decision of *Dodge v Ford* 170 N.W. 668 (Mich. 1919).

⁷ The debate has generated an extensive body of research, by no means limited to the sources that will be discussed and referenced in this chapter. See for example: Andrew Keay *The Enlightened Shareholder Value Principle and Corporate Governance* (Routledge 2013); Simon Deakin 'The Coming Transformation of Shareholder Value' (2005) 13(1) *Corporate Governance: An International Review* 11; Deryn Fisher 'The enlightened shareholder - leaving stakeholders in the dark: will section 172(1) of the Companies Act 2006 make directors consider the impact of their decisions on third parties?' (2009) 20(1) *ICCLR*10; R. Edward Freeman, Andrew C. Wicks and Bidhan Parmar 'Stakeholder Theory and "The Corporate

The analysis in this chapter will show how societal and legal norms have been moving slowly in a more stakeholder-centric direction. In spite of this, the existing legal position still focusses on the interests of the company's shareholders and maximising wealth and shareholder return remains the dominant corporate objective.⁸ For purposes of this thesis, these issues are key as many corporate governance codes tend to be more aspirational where stakeholder interests are concerned.

King IV advocates strongly for a more pluralists approach to the interests of the company, as did its predecessor King III.⁹ Should this approach be adopted by the courts, it may well push the South African legal position robustly in a pluralist direction. Given the position in various developed jurisdictions, it may be that this leap - though perhaps ultimately laudable - will be premature and unsustainable in practice.¹⁰

This chapter will offer an overview of the stakeholder debate to the extent required to illustrate its impact on the duty of the company director to act in the best interests of the company (or more lately in the case of the UK to promote the success of the company).¹¹ This duty and its application and interpretation is significant to the thesis as, together with the duty of care and skill, it serves to illustrate in a practical sense how an interpretation of directors' duties incorporating principles from governance codes may impact existing law. To do so, the chapter will also consider the context and

Objective Revisited" (2004) 15(3) *Organization Science* 364; Sundaram and Inkpen (n5) 350.

⁸ Keay (n7) 16. Keay notes that this might amongst other things be attributable to so-called 'path-dependence theory' which contends essentially that persistent differences in corporate rules and structures from one economy to the next are the result of the structures that were initially in place. See: Lucian Arye Bebchuk and Mark J. Roe 'A Theory of Path Dependence in Corporate Ownership and Governance' (1999) 52(172) *Stan.L.Rev* 127.

⁹ See further discussion below.

¹⁰ These more normative questions will be considered again in chapters 6 and 7 of the thesis.

¹¹ The debate has generated a vast amount of literature and to do it justice would require one to devote an entire thesis to it. An overview of these sources is provided in the references below.

development of the duty to act in the interests of the company and what form it takes in current law. Finally, the contents of especially King IV will be considered to predict any impact it may have on the existing legal position and highlight potential pitfalls that its application may have.

2 A Phrase with many Meanings – The ‘Corporate Objective’ and the Stakeholder Debate

Views on what should be the primary focus or responsibility for company directors when directing the companies that they serve have leaned in one direction or the other, depending on how the corporation as an entity was perceived at the time. Although there are variants on the general themes, three dominant schools of thought have emerged. The first, known as the ‘shareholder value’ theory¹² provides that the directors are to manage the company to ensure the fullest maximisation of shareholder wealth. In a nutshell, it implies that the managers have exclusively economic goals and ‘may do anything to enhance shareholder wealth provided that it is lawful.’¹³ At the other end of the spectrum, is the so called ‘stakeholder theory’, which contends at its core that there are others, besides shareholders, who are worthy of protection as they too are affected by the actions of the company. The thinking is that the loyalty that the fair treatment of stakeholders inspires will result in improved returns for shareholders down the line as it would benefit the company while also creating greater social wealth.¹⁴

¹² The theory is also known as ‘shareholder primacy’ or ‘shareholder wealth maximisation’. See: Keay (n7) 16 and see further discussion below and sources cited.

¹³ Keay (n7) 17. And see Wen (n5) 305.

¹⁴ Keay (n7) 43. And see: Tricker (n1) 75, where the author explains that: “Stakeholder thinking is concerned with values and beliefs about the appropriate relationships between the individual, the enterprise, and the state. It involves a discourse on the balance of responsibility, accountability, and power throughout society.” See also:

The third option, which was embraced by the Company Law Review Steering Group and subsequently the legislature in the United Kingdom, is referred to as the 'enlightened shareholder value principle'.¹⁵ In terms of this approach, the directors must continue to manage the company with shareholder value as the ultimate goal. However, enlightened shareholder value determines that directors must, where appropriate, also 'have regard to the need to build long-term and trusting relationships with employees, suppliers, customers and others in order to secure the success of the enterprise over time.'¹⁶

Shareholder primacy, or profit maximisation has been the favoured approach in the field of finance, where its logic is such that texts merely assert it as fact without debating any alternatives.¹⁷ Divergent opinions have come from management and strategy scholars who have argued on the one hand that governance should be stakeholder oriented or on the other that corporations should balance multiple goals,¹⁸ while legal scholars have questioned the popular acceptance of shareholder primacy as a norm in

¹⁵ Company Law Review Steering Group *Modern Company Law for a Competitive Economy: Strategic Framework* (1999 DTI) par 5.1.22. And see Keay (n7) 43; Clarke (n11) 50.

¹⁶ Company Law Review Steering Group *Modern Company Law for a Competitive Economy: Strategic Framework* (1999 DTI) par 5.1.22.

¹⁷ Sundaram and Inkpen (n5) 350, where the authors point out that, in the context of the financial field, "[d]eviation from this objective is cast as an agency problem resulting from the separation of ownership and control, and failure to meet this goal is assumed to be corrected by corporate boards, shareholder voice, shareholder exit, and the market for corporate control."

¹⁸ Sundaram and Inkpen (n5) 350. The authors cite as examples of the former Freeman, R. E., J. McVea. 2001. A stakeholder approach to strategic management. M. Hitt, E. Freeman, J. Harrison, eds. *Handbook of Strategic Management*. Blackwell Publishing, Oxford, U.K., 189–207. As examples of the latter they point to Drucker, P. 2001. The next society: A survey of the near future. *The Economist* (November 3) 1–20 and Quinn, J. B. 1980. *Strategies for Change: Logical Incrementalism*. Richard D. Irwin Inc., Homewood, IL. And cf Freeman and others (n7) 364 for a critique of Sundaram & Inkpen's views as expressed in 'The Corporate Objective Revisited' above.

company law for some time.¹⁹ The following paragraphs will offer an overview of how these theories have developed and will briefly consider the contents, strengths and weaknesses of each approach.

a. Shareholder Value

Initially, while incorporation was still dependent upon government charter, the corporation (as a creation of the state) was considered ‘a useful instrument for the state to carry out its public policy goals and as an entity whose powers must be kept in check.’²⁰ As the ability of the regulator to dictate corporate objectives waned, the pendulum swung away from the protection of stakeholders towards a managerial approach emphasizing shareholder wealth.²¹

The idea that the interests of the company are defined as the interests of its members mirrored the argument that the preferred objective function for the nominal corporation should be to optimise shareholder value.²² In the United States this was articulated most clearly by the Michigan State supreme court in the famous decision of *Dodge vs Ford Motor Company*²³ decided in 1919. The court concluded unequivocally that ‘[t]he business corporation is organized and carried on primarily for the profit of

¹⁹ See: Deakin (n7) 11; Jonathan Mukwiri ‘Myth of Shareholder Primacy in English Law’ (2013) *European Business Law Review* 217; Jim Apollo Mathiopoulos ‘The purpose of for profit corporations in light of modern perceptions and wider corporate responsibilities (Part 1)’ (2017) 38(9) *Co Law* 278.

²⁰ This explains the emphasis on and importance of the ultra vires doctrine which was gradually undermined as general incorporation resulted in a great number of new companies pursuing private agendas. Sundaram and Inkpen (n5) 351. And on the history of the company in general see chapter 1.

²¹ Sundaram and Inkpen (n5) 351. See also: William Lazonick & Mary O’Sullivan ‘Maximizing shareholder value: a new ideology for corporate governance’ (2000) 29(1) *Economy and Society* 13.

²² *Hutton v West Cork Railway Co* (1883) L.R. 23 Ch. D. 654 Ch D. is often cited as authority for this proposition but cf Mukwiri (n19) 217.

²³ *Dodge vs Ford Motor Company* 204 Mich. 459.

stockholders. The powers of the directors are to be employed for that end.’²⁴ From an English context, Bowen LJ famously observed that ‘the law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company.’²⁵ The statement could be construed to imply that any cakes and ale to be handed out must somehow benefit the company’s financial bottom line; gratuitous charity with no discernible returns would not be acceptable.²⁶

Debates about companies’ responsibilities in the context of public regulation of the economy came to the fore especially in the wake of the 1929 depression. Berle famously argued that the solution lies in handing back control to shareholders,²⁷ while counter arguments pointed out that dispersed ownership undermines the efficiency of the shareholder’s monitoring function. The solution that emerged was a combination of managerial and public control over companies. Privatisation and the deregulation of areas of the economy during the 1970’s led especially finance scholars to argue that the managers of large corporations should be controlled by the market in the first place – realising that ‘dispersed share ownership ... freed management from direct supervision by investors.’²⁸ However, the 1998 UK Hampel Committee report reiterated the status quo by concluding that ‘directors are responsible for relations with stakeholders, but are accountable to the shareholders’.²⁹

²⁴ *Dodge vs Ford Motor Company* 204 Mich. 459 at 507.

²⁵ *Hutton v West Cork Railway* (1883) 23 Ch. D. at 673. The case was decided in the context of the ultra vires principle, but the ‘benefit of the company’ that the court refers to, alludes very clearly to commercial success or viability.

²⁶ In a similar vein see *Re W&M Roith Ltd* [1967] 1 W.L.R. 432 and cf *Lindgren v L&P Estates Ltd* [1968] 1 All ER 917 where directors were found to have adequately considered the commercial merits of their decision despite it potentially taking many years for any benefit to materialise.

²⁷ Berle, A. (1932) For Whom Corporate Managers Are Trustees: A Note, *HarvLRev*, 45, 1365. The argument was most notably put forth in his debate with Dodd. See also: Dodd, E. M. (1932) For Whom are Corporate Managers Trustees? *HarvLRev*, 45, 1145.

²⁸ Deakin (n7) 13.

²⁹ Tricker (n1) 77.

As this overview illustrates, there has been a tussle between proponents of stakeholder theory and the concept of shareholder primacy for some time. If debacles such as those related to Enron and Worldcom at the turn of the century called shareholder primacy into question,³⁰ the financial crisis only compounded existing doubt. One might indeed conclude that '[a]lthough shareholder primacy is not dead by any stretch, it has suffered a series of blows that render it open to serious question.'³¹ Some authors have questioned the legitimacy of the theory as a staple of English law,³² while others have scrutinised the purported advantages of the approach.³³

Deakin argued more than a decade ago that the origins of shareholder primacy lie outside the core of company law and that instead it was founded by the norms and practices that marked the 1970s/1980s hostile takeover movement in the United Kingdom and America.³⁴ If one then sees shareholder primacy as an essentially cultural point of reference as opposed to a legal one, it is clearly not as 'institutionalised' as one might think.³⁵ In support for this argument, the author notes that company law itself actually does little to support the notion of shareholder primacy. It is justified neither by ownership theory³⁶ nor by the manner in which directors' duties are

³⁰ See for example: William W Bratton 'Enron and the Dark Side of Shareholder Value' (2002) 76 *Tul.L.Rev* 1275.

³¹ Matthew T Bodie 'The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm' (2012) 35 *Seattle U. L. Rev.* 1039.

³² For example see: Deakin (n7) 11; Mukwiri (n19) 217.

³³ Keay (n7) 20 – 41 where the author provides a comprehensive overview of the strengths and weaknesses of the theory.

³⁴ Deakin (n7) 16. Deakin illustrates how many of the responses to the takeover movement were internalised and subsequently became entrenched to ensure that senior management identified strongly with the goal of maximising share price.

³⁵ Deakin (n7) 16.

³⁶ Deakin (n7) 12. The idea could not be rooted in the fact that the shareholders 'own the company' because of course it is not clear in what sense they could 'own' what is essentially a fictive legal entity that owes its existence to the act of incorporation. Furthermore, owning a share does not entitle a shareholder to any particular segment of the company's assets (at least not as long as the entity is operating as a going concern). See also: Blanaid Clarke 'Corporate responsibility in light of the separation of ownership and control' (1997) 19 *Dublin University Law Journal* 50.

legally constructed as any fiduciary duties are owed the company, and not its shareholders directly.³⁷ Company law also does not guarantee any level of returns that shareholders could insist on, nor does it offer a time scale in line with which shareholder expectations are to be realised.³⁸ Deakin concluded that '[t]he current focus on shareholder value is ... the consequence not of the basic company law model, but of those institutional changes which have occurred in capital markets and securities law ... in particular since the early 1980s'.³⁹

Mukwiri also questioned the validity of the assumption that shareholder primacy was the norm in English law preceding the 2006 Companies Act, by reconsidering the caselaw long thought to have underpinned the theory. In doing so, he concluded that 'the confusion was based on the historical application of partnership principles to company law, and that a contextual reading of case law reveals that shareholder primacy is at odds with the tenet of corporate legal personality.'⁴⁰ The author points out that, as English company law had its roots in partnership law, principles from the latter permeated company law for the early years of its development until legal personality became a firmly entrenched concept. Of course, the pivotal difference where partnerships are concerned, lies in the fact that the

³⁷ Deakin (n7) 12 where the author explains that this is more than a mere rhetorical device: 'In practice, the company's interests will often be synonymous with those of its members, that is, the shareholders. However, shareholders are not entitled to engage directly in the management of the enterprise; this is the responsibility of the board.'

³⁸ Deakin (n7) 12. One of the strongest counter arguments advanced by agency theory, is the fact that although shareholders may not 'own' the company in the legal or technical sense, 'ownership of shares confers upon them the right, exclusively of all the stakeholder groups, to hold directors and managers accountable.' However, this does not hold sway as agency theory does not justify shareholders' right to hold managers accountable by means of an ownership claim, but instead bases it on the notion that it is in the best interests of society that they should do so. Deakin (n7) 12.

³⁹ Deakin (n7) 14.

⁴⁰ Mukwiri (n19) 218.

partners are direct owners of the assets of the partnership and this also formed the basis for their entitlements and rights to control the entity. Once separate legal personality was fully entrenched in legal precedent one might have expected shareholder primacy to have been abandoned as contrary to the tenets of company law, but this was not the case. The 'ownership myth and the legal remnants which sustain it' have resulted in a 'hangover from earlier times' in terms of which shareholder primacy was erroneously assumed to form the basis of corporate governance in English company law.⁴¹ In light of this, Mukwiri proposed that case law following the decision in *Salomon*⁴² should be interpreted in light of separate legal personality unless they 'unequivocally promote shareholder primacy'⁴³ and cautions that section 172 should not be interpreted through the prism of this theory.

In contrast, Blackman pointed out that the principle of shareholder primacy does not mean to suggest that the company and its members are one and the same – this would be anathema to company law. It is based instead on the attribution of the interests of the shareholders to the company, a principle of company law which contends that 'in law, the company's interests are the interests of its shareholders *qua* shareholders, ie their interests in the prosperity of the company as a business concern.'⁴⁴ In other words, '[t]he interests of a company, an artificial person, cannot be distinguished from the interests of the persons who are interested in it'.⁴⁵

⁴¹ Mukwiri (n19) 220 citing P Ireland, *Company Law and the Myth of Shareholder Ownership* 62 MLR 32, 48 (1999) and S Worthington, *Shares and Shareholders: Property, Power and Entitlement (Part 1)* 22 Co Law 258, 259 (2001).

⁴² [1897] AC 22.

⁴³ Mukwiri (n19) 220.

⁴⁴ Revision Service 12 (2012) Ch 8 – 70.

⁴⁵ *Brady v Brady* [1988] BCLC 20 40 (CA). Blackman also points out that 'the argument that the identification of the shareholders' interests to the company is mistaken is usually coupled with the claim that the law ought not to recognise only the interests of the shareholders as the interests of the company, ie that the law ought also to recognise the interests of other persons. This, of course, is not an argument that the attribution of the members' interests to the company is a jurisprudential mistake, or that the company as such has interests of its own, but

The author also notes that the argument is usually made in support of a more inclusive approach to stakeholder interests which is more accurately a policy argument and not one based on the idea that ‘the attribution of the members’ interests to the company is a jurisprudential mistake, or that the company as such has interests of its own’⁴⁶ although it is difficult to see how this is not exactly what the authors above have implied.

There are several other doctrinal and conceptual criticism that have been raised against the notion of shareholder value. A discussion of all these points falls outside the scope of this research and will not serve to further inform the research question. Keay offers a comprehensive overview. Amongst other things he points out that shareholder value rests in large part on mistaken perceptions that the directors act as agents of the shareholders, that shareholders are the ones who actually bear the residual risk, that the maximisation of shareholder wealth would serve to increase efficiency and concomitantly enhanced social wealth, and importantly, that shareholder value offers a greater degree of certainty than does stakeholder theory.⁴⁷

an argument of policy about the persons whose interests ought to be attributed to the company.’ Blackman’s Commentary (Revision Service 12 2012) Ch 8 – 70.

⁴⁶ Revision Service 12 (2012) Ch 8 – 70.

⁴⁷ Keay (n7) 20 – 25. And see: Lynn Stout ‘Bad and Not-So-Bad Arguments for Shareholder Primacy’ (2002) 75 *Southern California Law Review* 1189; Daniel T.Y. Cheung ‘A discussion on whether there is justification in incorporating a stakeholder theory into UK corporate governance for private companies in unregulated transactions’ (2018) 39(10) *Co Law* 315, 317; Cheryl C. Asher, Joseph Mahoney and James Mahoney ‘Towards a Property Rights Foundation for a Stakeholder Theory of the Firm’ (2005) 9 *Journal of Management and Governance* 5, 29–32; C Bagley & K Page ‘The Devil Made Me Do It: Replacing Corporate Directors’ Veil of Secrecy with the Mantle of Stewardship’ (1999) 36 *San Diego Law Review* 897; Min Yan ‘The Corporate Objective Revisited: Part 1’ (2017) 38(1) *Business Law Review* available online at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2947962 [accessed on 12/04/2018]; P Ireland ‘Company Law and the Myth of Shareholder Ownership’ (1999) 62 *Modern Law Review* 32. But cf Lorraine Talbot ‘Trying to save the world with company law? Some problems’ (2016) 36(3) *Legal Studies* 513, 513 where the author cautions that ‘critical scholars have cohered around a core claim about company law which is erroneous. Furthermore, they have largely assumed that the current economy can sustain a social agenda as well as creating profit. This ... hugely underestimates entrenched problems in the economy’.

Finally, in defence of shareholder primacy, Wen points out that to the extent that the theory is perceived as immoral and short-sighted, this is due to a misunderstanding of its application in English law and that it is in fact neither.⁴⁸ This, the author argues, is due to the fact that the interests of the shareholders have always been interpreted as encompassing the interests of the shareholders present and future and '[t]he logic lies in that the goal of long-term shareholder value can only be successfully pursued by developing sustaining relationships with stakeholders.'⁴⁹

Kay referenced an ironic anecdote in relation to the shareholder value proposition:

Jack Welch of General Electric is widely credited with inaugurating that era in a speech at the Pierre Hotel in New York soon after he took over as that company's CEO. Welch did not in fact use the phrase 'shareholder value', but it became more and more widely heard in the two decades that followed. Only in 2009, some years into retirement, would Welch describe shareholder value as 'the dumbest idea in the world'.⁵⁰

It may be criticised; it may perhaps even be 'the dumbest idea in the world' but its influence has been, and remains pervasive.

b. The Stakeholder Approach

At the opposite end of the spectrum, is the so-called stakeholder approach.⁵¹ Germany and Japan are considered to have fully embraced this strategy

⁴⁸ Wen (n5) 314.

⁴⁹ Wen (n5) 314.

⁵⁰ John Kay 'Theories of the Firm' (2018) 25(1) *International Journal of the Economics of Business* 13 citing in turn Welch, Jack. 1982. "Growing Fast in a Slow Growth Economy." <http://www.123helpme.com/jackwelch-view.asp?id=160218andWelch,Jack.2009>. <https://www.ft.com/content/294ff1f2-0f27-11de-ba10-0000779fd2ac>

⁵¹ Keay (n7) 16. See also: RE Freeman & R Phillips 'Stakeholder Theory: A Libertarian Defence' (2002) 12 *BEQ* 331; R Karmel 'Implications of the Stakeholder Model' (1993) 61 *Geo.Wash.L.Rev.* 1156; K Greenfield 'Saving the World With Corporate Law' (2008) 57 *Emory LJ* 947; A Keay 'Stakeholder Theory in Corporate Law: Has It

which rests essentially on two pillars. First, the idea that more than just the shareholders contribute to the company and its success and are concomitantly affected by its actions; and second a complete lack of commitment to other stakeholders will lead to a lack of loyalty on the part of other constituents when the company direly requires it.⁵² Also referred to as pluralism or the pluralist approach, the theory is not new. Although a 1975 discussion paper by the UK Accounting Standards Steering Committee, recommended that all large economic entities should produce accountability reports to all stakeholder groups at regular intervals, it was a lone voice in the wilderness and ‘the political implications of such a heroic idea quickly relegated the report to the archives.’⁵³ Besides this, Ralph Nader, clashed with the ‘boardroom oriented’ Business Roundtable during the 1970s, and together with Mark Green and Joel Seligman, pointed out that big companies potentially have enormous power, yet to a large extent remain unaccountable to their constituencies.⁵⁴ However, the ‘father of modern stakeholder theory’ is considered to be R Edward Freeman, who proposed the main thrust of the theory in his 1984 book entitled *Strategic Management: A Stakeholder Approach*.⁵⁵

A good example of this new way of thinking is the 1999 report prepared by the Royal Society of Arts in England, entitled ‘Tomorrow’s Company’.⁵⁶ The committee preparing the report was chaired by Sir Stuart Hampson who remarked at the time: ‘We don’t believe that the board is there purely to

Got What It Takes?’ (2010) 9 *Rich. J. Global L. & Bus.* 249; A Campbell ‘Stakeholders, the Case in Favour’ (1997) 30 *LRP* 446; Cheung (n47) 316; Kevin Gibson ‘The Moral Basis for Stakeholder Theory’ (2000) 26(3) *JBE* 245.

⁵² Keay (n7) 43. And see: C Leadbeater, ‘Why it Pays to be Good (Eventually)’ (2000) *New Statesman* 26 available online at <https://www.newstatesman.com/node/193387> [accessed on 20/08/2019].

⁵³ Tricker (n1) 75.

⁵⁴ Tricker (n1) 75.

⁵⁵ R Edward Freeman *Strategic Management: A Stakeholder Approach* (Pitman/Ballinger 1984).

⁵⁶ Lynn Stout et al ‘The Modern Corporation Statement on Company Law’ (October 6, 2016). Available at SSRN: <https://ssrn.com/abstract=2848833>.

create shareholder value. I'm sure nobody leaps out of bed in the morning and says 'I want to create shareholder value!' It's unrealistic'.⁵⁷

This does not mean to say that a stakeholder approach does not present the company board with some rather obvious challenges.⁵⁸ What immediately comes to mind, for example, is how to deal with the inevitable conflicts of interests that are bound to arise when the interests of multiple constituents are taken into account.⁵⁹ Critics also point out that it is impossible to maximise all stakeholder interests at the same time, interests within stakeholder groups may vary which will add to the complexity, and it is undefined who is supposed to establish the interests within each group.⁶⁰ Yet this very fact may well be one of the strengths of pluralism, as 'stakeholder theorists will often argue that because this theory has concern for a wider range of groups, it takes in the complexity of the world, whereas shareholder value, with its focus on a single objective is far too glib.'⁶¹ To counter challenges posed by conflicting interests it is suggested that

⁵⁷ Tricker (n1) 76. The European response was highlighted in a EC Directorate-General for Employment and Social Affairs Green Paper *Promoting a European Framework for Corporate Social Responsibility* (2001) available online at: Europa.eu>rapid>press-release DOC-01-9 en [accessed on 12/08/2019] and see in overview: Saleem Sheikh 'Promoting Corporate Social Responsibility Within the EU' (2002) *ICCLR*143; Copp Stephen 'Corporate governance: change, consistency and evolution: Part 1' (2003) 14(2) *ICCLR*65. See also: Freeman and others (n7) 365 where the authors contend that 'stakeholder theory does a better job of explaining and directing managerial behavior (sic) in markets'.

⁵⁸ See for an overview of criticisms for example: Min Yan 'Why not stakeholder theory?' (2013) 34(5) *Co Law* 148.

⁵⁹ Sternberg contended that these conflicts could not be reconciled and that directors should be able to focus on a single responsibility, that which they owe to their shareholder. Elaine Sternberg, 'The Stakeholder Concept: A Mistaken Doctrine' (1999) *Foundation for Business Responsibilities, Issue Paper No.4* Available online at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=263144 [Accessed 6 July 2019]. But cf Shann Turnbull 'Stakeholder Governance: A Cybernetic and property Rights Analysis in Corporate Governance' (1997) 5(1) *CG* 11 – 23.

⁶⁰ Tricker (n1) 76. And see Eric Pichet 'Enlightened Shareholder Theory: Whose Interests Should Be Served by the Supporters of Corporate Governance?' (2011) 8 *Corporate Ownership & Control* 353; 358.

⁶¹ Keay (n7) 46; Freeman and others (n7) 365.

directors should engage in a balancing exercise which appears to be a viable but not infallible suggestion.⁶²

Pluralism was rejected by the Company Law Review Steering Group on the basis that 'if there are deficiencies in this area they are best made good by changes in other areas of the law and public policy, or in best practice, rather than by making changes in company law, which might have unpredictable and damaging effects'.⁶³ Furthermore, the Steering Group was concerned that the variable number of interests that had to be taken into account would give directors a discretion that would be impossible to police and might 'dangerously distract management into a political balancing style at the expense of economic growth and international competitiveness'.⁶⁴ In particular, the Steering Group opposed pluralism for reasons that are pertinent to the arguments considered by this research, namely because:

In particular ... this would impose a distributive economic role on directors in allocating the benefits and burdens of management of the company's resources; that this role would be uncontrolled if left to director's in the form of a power or discretion; and that a similarly broad role would be imposed on the judges if the new arrangement took the form of an enforceable obligation conferring rights on all the interested parties to argue for their interests in court.⁶⁵

⁶² Keay (n7) 46. Keay highlights other criticisms levelled against the theory; such as the fact that it lacks normative foundations, that the concepts which underpin it are unclear, that enforcement is problematic and that it does not result in fairer outcomes at pages 49 – 52. For a comprehensive critique of the business case for stakeholder rights see also: Michael L Barnett (ed) *Limits to Stakeholder Influence: Why the Business Case Won't Save the World* (Edward Elgar 2018) and for additional retorts to the criticism pointed out above see: Freeman and others (n7) 364.

⁶³ Department of Trade and Industry *Modern Company Law for a Competitive Economy: The Strategic Framework* (1999) par 5.1.27.

⁶⁴ Department of Trade and Industry *Modern Company Law for a Competitive Economy: The Strategic Framework* (1999) par 5.1.27.

⁶⁵ Company Law Review Steering Group *Modern Company Law for a Competitive Economy: Developing the Framework* (DTI 2000) at para 5.1.28.

As mentioned above, these are likely the dominant concerns that would arise if King IV were to inform the duty to act in the best interests of the company more robustly.⁶⁶ It is perhaps especially prevalent given the past injustices and the resulting socio-economic inequalities that still plague South African society.⁶⁷ As chapter 5 in particular will argue, it highlights one of the most pertinent concerns when requiring the courts to interpret directors duties taking cognisance of King IV and thus indirectly also of multiple stakeholders. It may well require the courts to make high level policy judgements without the information or access to the ‘bigger picture’ that is required to do so.⁶⁸ In the context of the United Kingdom Talbot has questioned whether the economy would prove able to absorb this more robust approach.⁶⁹ Similar concerns are certainly warranted in the South African context where especial caution is warranted when developing this area of the law.

c. **Enlightened Shareholder Value**

Having rejected pure stakeholder theory, the legislature in the UK opted instead to endorse a so-called ‘enlightened shareholder value’ approach.⁷⁰ It was first proposed by one of the greatest proponents of shareholder value, Michael Jensen, at the turn of the century.⁷¹ Jensen’s theory was an attempt

⁶⁶ See further discussion below at text to note 142 and onwards.

⁶⁷ This issue will be debated further below in chapter 8.

⁶⁸ See chapter 5 text to note 180.

⁶⁹ Lorraine Talbot ‘Trying to save the world with company law? Some problems’ (2016) 36(3) *LS* 513.

⁷⁰ For a comprehensive analysis of this approach see: Keay (n7). See also: Fisher (n7) 10; Joan Loughrey; Andrew Keay; Luca Cerioni, ‘Legal Practitioners, Enlightened Shareholder Value and the Shaping of Corporate Governance’ (2008) 8 *J. Corp. Law Stud.* 79; Elaine Lynch ‘Section 172: a ground-breaking reform of director’s duties, or the emperor’s new clothes?’ (2012) 33(7) *Co Law* 196; Andrew Johnston ‘After the OFR: can UK shareholder value still be enlightened? (2006) 7(4) *EBOR* 817.

⁷¹ Michael Jensen ‘Value Maximisation, Stakeholder Theory and the Corporate Objective Function’ (2001) 7(3) *EFM* 297.

to show the ‘proper relation between value maximisation and stakeholder theory, termed ‘enlightened value maximisation’.⁷² Jensen criticised stakeholder theory’s lack of focus and contended that it undermined value creation. At the same time, he acknowledged that firms would not be able to maximise value if they ignore stakeholder interests. The theory does not mark a firm departure from the shareholder primacy model, but it does insist that in creating long term value directors must ‘make the requisite tradeoffs among ... stakeholders’.⁷³ An apparently broader approach formed the Enlightened Shareholder Value approach which was finally embraced by the Steering Group and eventually informed the formulation of the duty contained in section 172 of the 2006 UK Companies Act.⁷⁴ The approach, as adopted into English and ostensibly South African law is considered further below as part of the current legal status. Though the approach is not without fault, it is the latest attempt to strike an illusive balance in an arena where so many interests conflict.⁷⁵

3 The Duty to Act in the Best Interests of the Company – The Position Prior to Codification

As with the duty to act with care, skill and diligence, South African law governing directors’ fiduciary duties was strongly informed by English law.⁷⁶ South African common law has always required the director to act ‘*bona fide* in the interests of the company as a whole.’⁷⁷ The court may intervene

⁷² Jensen ‘Value Maximisation’ (n71) 299.

⁷³ Jensen ‘Value Maximisation’ (n71) 297.

⁷⁴ Keay (n7) 63. And see: Johnston (n70) 827.

⁷⁵ Janice Dean ‘The future of U.K. company law’ (2001) 22(4) *Co Law* 104, 104.

⁷⁶ See chapter 1 text to note 116 – note 123.

⁷⁷ The principle was described as ‘indisputable’ by Ogilvie Thompson CJ in *South African Fabrics Ltd v Millman, NO, and Another* 1972 (4) SA 592 at 596. See also: *Harcourt v Eastman, N.O.*, 1953 (2) SA 424 (N) at pp. 428 429; *Marshall Industrials Ltd. v Khan*, 1959 (4) SA at p. 694.

based on the fact that the director was appointed to act on behalf of the company, and if he then acts in either his own interests or those of some other third party or parties he is acting improperly, or for an improper purpose.⁷⁸ These duties become alive whenever the directors exercise their powers or discretion relating to the management of the affairs of the company.

Common law did not limit liability to instances where there was some or other action but extended under certain circumstances to omissions;⁷⁹ for example not attending a meeting despite a responsibility to inform the rest of the board of certain facts or failing to vote where a director should have voted in order to act in the company's best interests.⁸⁰ It would appear that even the act of resignation may, under certain circumstances, be considered to have been in bad faith and can constitute a breach of fiduciary duty. This was the case in *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Co Ltd*⁸¹ where all the directors of a public company chose to resign *en masse*. The court in this case found that there were no reasonable grounds for the mass resignation and that the directors had not acted in good faith by doing so. Having accepted the duties and obligations that go with their appointment as directors, it was irresponsible for them to abandon the company, and they could not 'be allowed to merely walk away because it was convenient to do so.'⁸²

⁷⁸ *South African Fabrics Ltd v Millman, NO, and Another* 1972 (4) SA 592 at 596;

⁷⁹ See eg *Harris v North Devon Railway Co* (1855) 20 Beav 52 ER 651 652; *Re National Provincial Marine Insurance Co (Gilbert's Case)* (1876) 5 Ch App 559 566.

⁸⁰ *Permanent Building Society v McGee* (1993) 11 ACSR 260 289-290 SC (WA); on appeal, *Permanent Building Society v Wheeler* (1994) 14 ACSR 109 160 SC(WA); *Fitzsimmons v R* (1997) 23 ACSR 355 358 SC(WA); *Duke Group Ltd v Pilmer* (1999) 31 ACSR 213 340-341 SC(WA). And see *Darvall v North Sydney Brick & Tile Co Ltd* (1989) 15 ACLR 230 250 CA(NSW).

⁸¹ 2006 (5) SA 333 (W).

⁸² *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Co Ltd* 2006 (5) SA 333 (W) at 351. In this instance, the company had been cited for violating its environmental obligations under section 24 of the Constitution of the Republic of South Africa and the court stressed that allowing such a resignation would make it

As far as the common law is concerned, the duty to act in good faith and the duty to act in the best interests of the company were technically considered two separate duties, although the courts have not applied the distinction consistently.⁸³ Blackman, however, describes the duties as a single test with two components, explaining that it is 'subjective as to means (what is to be done in order to promote the company's interests), but objective as to ends (the interests to be promoted, ie 'the interests of the company').'⁸⁴

The 'subjective'⁸⁵ component of the test, emphasises yet again that directors have some autonomy to act in what they honestly perceive to be the best interests of the company. The courts have reiterated that it is the honest opinion of the directors that is at stake, and not the opinion that the courts may be inclined to reach after the fact.⁸⁶ Centlivres CJ went as far as to conclude that 'in the absence of any allegation that the directors acted *mala fide* this amounts to asking [the] Court to usurp the functions of the directors and to consider what is the best for the company from the business point of view. This is not the function of a Court of law.'⁸⁷ In support, the judge cites English law, referring to amongst others, the remarks of Lord Loreburn L.C who concluded that '[i]t is no part of the business of a Court of justice to determine the wisdom of a course adopted by a company in the management of its own affairs'.⁸⁸ Or, as Lord Greene MR simply put it in *Re*

difficult for courts to enforce an order *at factum praestandum* against a company by means of a punitive order.

⁸³ *Silva v CH Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA) para 18.

⁸⁴ Blackman ch8 -62

⁸⁵ *per* Nourse LJ in *Brady v Brady* [1988] BCLC 20 41 (CA).

⁸⁶ *Ngurli Ltd v McCann* (1953) 90 CLR 425 438 (HC of A); *Russell Kinsela Pty Ltd v Kinsela* (1983) 8 ACLR 384 403 SC (NSW).

⁸⁷ *Levin v Felt & Tweeds Ltd* 1951 (2) SA 402 (AD) at 415.

⁸⁸ *Poole v National Bank of China Ltd.*, 1907 AC 229 at 236. Centlivres CJ referred also to the case of *Caldwell & Co. Ltd v Caldwell*, 53 Sc LR 251 at 253, where Lord Shaw in the House of Lords approved of the following remarks made by Lord Skerrington: 'I cannot find any trace in the statute of a suggestion that the Court ought to review the opinion of the company and its directors in regard to a question which primarily at least is domestic and commercial.'

*Smith & Fawcett Ltd*⁸⁹ the directors should act ‘bona fide in what they consider – not what a court may consider – is in the interests of the company’.⁹⁰

To the extent that the director is required to act ‘in the interests of the company’ on the other hand, the inquiry is framed more objectively. Despite his belief that he was acting in the company’s best interests, liability would follow at common law if he was not *actually* doing so and had misunderstood or misconstrued the company’s ‘best interests’.⁹¹

In the case of the duty to act in the best interests of the company, the South African courts, like their English counterparts, interpreted the ‘best interests of the company’ with a pronounced focus on the shareholders and shareholder interests. The approach accorded with the prevailing sentiment at the time – namely that the company is a creature with profit as its primary goal (profit maximisation).⁹² If, in other words, one considers the director’s duty to act in the best interests of the company, the popular view was consistently that the best interests of the company are the interests of the shareholders⁹³ (in their capacity as such) as a body.⁹⁴

⁸⁹ [1942] Ch. 304.

⁹⁰ [1942] Ch. 304 at 306 CA.

⁹¹ Blackman Ch 8 page 70.

⁹² See discussion above in paragraph a.

⁹³ This includes both present and future members, see: *Gaiman v National Association for Mental Health* [1971] Ch. At 330.

⁹⁴ Yeats JL and others, *Commentary on the Companies Act of 2008* (Juta 2017) Revision Service 12 (2012) ch8 – 69 where the authors point out that this must necessarily be so as one could not argue that the fictitious entity had any interests that were particularly its own; see also in this regard Davies PL & Worthington S *Gower’s Principles of Modern Company Law* (10th edn Sweet & Maxwell 2016) 502, and *cf* the following statement by Hussain J seemingly implying that the corporate entity has its own interests, apart from the interests of its members: ‘The ‘interests’ in this context, are only those of the company itself as a corporate entity and those of its members as a body’ *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Co Ltd* 2006 (5) SA 333 (W) at 350.

4 The Existing Legal Position

a. Current Position in the UK

As discussed in Chapter 1 above, the Companies Act of 2006 codified all directors' duties, including the common law duty to act in the best interests of the company. Section 172 now states that a director should act 'in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole'.⁹⁵ In doing so, the 2006 Act specifically requires said director to 'have regard' to six matters listed in the section, namely:⁹⁶

- (a) the likely consequences of any decision in the long term,
- (b) the interests of the company's employees,
- (c) the need to foster the company's business relationships with suppliers, customers and others,
- (d) the impact of the company's operations on the community and the environment,
- (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
- (f) the need to act fairly as between members of the company.

This revision of the common law test, referred to as 'enlightened shareholder value' by the Company Law Review Steering Group (CLRSG),⁹⁷

⁹⁵ S 172(1).

⁹⁶ S 172(1)(a) – (f). The list is not exhaustive.

⁹⁷ Company Law Review, *Modern Company Law for a Competitive Economy: Developing the Framework* (DTI, London, 2000), par. 2.22. And for an overview of the considerations considered at the time see: Sarah Kiarie 'At crossroads: shareholder value, stakeholder value and enlightened shareholder value: Which road should the United Kingdom take?' (2006) 17(11) *ICCLR*329; Loughrey and others 'Legal Practitioners' (n70) 79.

represents a compromise between two extreme approaches. It is described by the committee in the following terms:

An obligation on directors to achieve the success of the company for the benefit of the shareholders by taking proper account of all the relevant considerations for that purpose ... [which would include] ... a proper balanced view of the short and long term, the need to sustain effective ongoing relationships with employees, customers, suppliers and others; and the need to maintain the company's reputation and to consider the impact of its operations on the community and the environment.⁹⁸

As mentioned, the committee thus chose to reject a pluralist approach that would see the rights of multiple stakeholders on an equal footing with the rights of shareholders – which would have to include the avenues for alternative stakeholders to somehow enforce directors' duties. The wording of the new section clearly leans more towards its common law predecessor in that it expressly requires directors to promote the success of the company 'for the benefit of its members'.⁹⁹ However, the statutory duty does evolve and refine shareholder primacy, by adding the abovementioned obligation to 'have regard to' the interests of other stakeholders. This begs the question whether directors are now merely to take account of the interests of (although, as Worthington and Davies point out this obligation is clearly subservient to the one that precedes it, which still requires 'shareholders or members ... to be the primary object of the directors' efforts.')¹⁰⁰ In other words, the directors are merely to take into account the interests of constituents to the extent that this promotes benefits to shareholders. They

⁹⁸ Company Law Review Steering Committee *Modern Company Law for a Competitive Economy: Developing the Framework* (DTI, London, 2000), par 2.19.

⁹⁹ Davies and Worthington (n520) 502.

¹⁰⁰ Davies and Worthington (n520) 502. Keay concurs with this interpretation based on both the background to the provision as well as the way in which it is drafted, see for example: Andrew Keay 'Section 172(1) of the Companies Act 2006: An Interpretation and Assessment' (2007) 28(4) *Co Law* 106 at 108. See also: John Lowry 'The Duty of Loyalty of Company Directors: Bridging the Accountability Gap through Efficient Disclosure' (2009) 68(3) *CLJ* 607, 618.

are not to concern themselves with such interests as ends in themselves. Their 'ultimate concern ... is that their action promotes the success of the company *for the benefit of the members as a whole*.'¹⁰¹

Davies and Worthington describe the modern version of the duty codified in the 2006 Companies Act as 'the most basic of the duties of good faith or fidelity owed by directors' and 'the core duty to which directors are subject, in the sense that it applies to every exercise of judgement which the directors undertake, whether they are testing the margins of their powers under the constitution or not and whether or not there is an operative conflict of interest.'¹⁰² They emphasise that '[t]ogether with the non-fiduciary duty to exercise care, skill and diligence, the duty to promote the success of the company expresses the law's view on how directors should discharge their functions on a day-to-day basis.'¹⁰³ The impact and interpretation of the section has since been considered by a number of commentators, most notably Prof Andrew Keay,¹⁰⁴ who pointed out that the discretion afforded to the directors is unfettered, with no objective criteria to assess what the directors have done.¹⁰⁵

¹⁰¹ Keay 'Section 172(1) of the Companies Act 2006' (n100) 108.

¹⁰² Davies and Worthington (n520) 501.

¹⁰³ Davies and Worthington (n520) 501.

¹⁰⁴ See for example: Andrew Keay 'Section 172(1) of the Companies Act 2006' (n100) 106.

¹⁰⁵ Keay 'Section 172(1) of the Companies Act 2006' (n100) 107. For example, the author notes that the section omits 'any reference to the fact that the directors are to consider the factors that a person of care and skill would consider relevant.' The section has been criticised by others. See for example: Nicholas Grier 'Enlightened shareholder value: did directors deliver?' (2014) 2 *Juridical Review* 95; David K Millon 'Enlightened Shareholder Value, Social Responsibility, and the Redefinition of Corporate Purpose Without Law' (2010) *Wash. & Lee Legal Studies Paper* No. 2010-11. Available at SSRN: <https://ssrn.com/abstract=1625750>; Lynch (n70) 196; David Milman 'Stakeholders in modern UK company law' (2017) 397 *C.L.N* 1, 4; Richard Williams, 'Enlightened Shareholder Value in UK Company Law' (2012) 35 *U.N.S.W.L.J.* 360, 362 where the author argues that enlightened shareholder value as embodied in section 172 does not represent any substantive change in the approach of UK company law to stakeholders and is not a useful model for other jurisdictions to emulate.

If one considers the matters that directors are required to take cognisance of in terms of the section, one can see how a board might be justified in considering provisions found in the UK Corporate Governance Code. This is due to the statutory mandate to ‘have regard to the desirability of the company maintaining a reputation for high standards of business conduct’.¹⁰⁶ However, even if one were to argue that reference to the voluntary codes that may apply to the company fall outside of the scope of this subsection, it is nonetheless clearly not an exhaustive list and it is hard to see how the provisions of these codes would not be a legitimate consideration when making decisions affecting the company. That being said, this remains a far cry from a legal *mandate* to consider provisions of the Governance Code.¹⁰⁷ If directors fail to do so, the section *could perhaps* be interpreted to require such reference, and if a failure to do so results in losses affecting the shareholders this may even hold some sway. However, the question then becomes whether the provisions of the code would significantly impact an assessment of the directors conduct and it is here where the position in the UK diverges from that in South Africa.¹⁰⁸

There have been notable developments in the United Kingdom, in the form of a Corporate Governance Reform Green Paper in November 2016, setting out ‘a new approach to strengthen big business through better corporate governance.’¹⁰⁹ The Green Paper set out three main areas for reform. First,

¹⁰⁶ See above at text to note 96.

¹⁰⁷ Fisher (n7) 15 where the author notes that possibility that ‘Parliament has created a right without a remedy, which the law abhors.’ And see: Lynch (n70) 200.

¹⁰⁸ This is perhaps an ironic consequence as the South African Act gives less express credence to stakeholder interests than does its English counterpart and yet a reading of the Act which would draw from King IV would have a far more pluralist consequence.

¹⁰⁹ BEIS: Corporate Governance Reform Green Paper (November 2016) available online at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/584013/corporate-governance-reform-green-paper.pdf accessed on 01/06/2018.

shareholder influence on executive pay; second, measures to increase the connection between boards of directors and other groups with an interest in corporate performance; and finally, 'whether some of the features of corporate governance that have worked well for listed companies should be extended to the largest privately-held companies'.¹¹⁰ Most recently a Corporate Governance Code for large private entities¹¹¹ has seen the light and secondary legislation now requires all companies of significant size to disclose their corporate governance arrangements.¹¹²

The Financial Reporting Council have also undertaken consultations with the eye on a proposed revision to the UK Corporate Governance Code and have been urged by ICSA to consider its alignment with the 2006 Companies Act.¹¹³ The revisions have also been criticised for their focus on a single stakeholder group (the workforce) and for the fact that the Code is not an appropriate tool for reporting compliance with section 172 of the Companies Act.¹¹⁴

¹¹⁰ BEIS: Corporate Governance Reform Green Paper (November 2016) at page 4. Available online at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/584013/corporate-governance-reform-green-paper.pdf accessed on 01/06/2018. For an overview of recent developments in the UK see: James McCalman & Angus Young 'Another round of corporate governance reforms in the UK: implications for directors in the financial sector' (2018) 33(8) *J.I.B.L.R.* 286.

¹¹¹ The Wates Corporate Governance Principles for Large Private Companies was issued by the FRC and took effect on 1 January 2019. Available online at: <https://www.frc.org.uk/getattachment/31dfb844-6d4b-4093-9bfe-19cee2c29cda/Wates-Corporate-Governance-Principles-for-LPC-Dec-2018.pdf> [accessed on]

¹¹² The Companies (Miscellaneous Reporting) Regulations 2018.

¹¹³ *Co Law* 'Corporate Governance Code needs to be more closely aligned with the Companies Act, says ICSA' (2018) 39(7) 220. For example, misalignment between section 172 and Principle A was highlighted in that the latter envisages a wider remit than the former.

¹¹⁴ Irene-Marie Esser & Iain MacNeil 'Proposed Revisions to the UK Corporate Governance Code: a step forward in recognising a company's responsibilities towards wider stakeholders?' (2018) 39(8) *Co Law* 254, 255. The authors point to the incoherent overlap between the requirements of the Code and the Provision 4 of the statutory strategic report requirements with both aimed at reporting on compliance with section 172. They also point out that inclusion in the Code seems

b. Current Position in South Africa

As discussed, section 67 of the Companies Act 71 of 2008 constitutes a partial codification of the common law relating to directors' duties and does not entirely supersede existing common law. This is not least because the duties set out in the Act are described in very broad terms, and the common law will likely still impact their interpretation.¹¹⁵ In terms of section 76(3)(c), a 'director of a company, when acting in that capacity, must exercise the powers and perform the functions of director ... in the best interests of the company...'

Thus, the section states merely that the directors must act in the best interests of the company, and 'the company' is not defined to now include a broader range of stakeholders. The 'interests' of the company are also not defined elsewhere in the Act, to give any greater degree of certainty. What is more, no express mention is made of stakeholder interests in the stated purposes of the Act, apart from the interests of stakeholders in the instance of financial distress and business rescue.¹¹⁶ There are some indications elsewhere in the legislation that the Act embodies a more progressive, and enlightened approach to stakeholder interests, but mostly this conclusion can be inferred from the aims of the legislation and context rather than any express provisions.

Perhaps the most notable step that the legislature took, is the creation of a mandatory social and ethics committee for certain companies.¹¹⁷ In terms of

odd in the face of secondary legislation which will require all companies to report on compliance with section 172.

¹¹⁵ See chapter 1 par # and chapter 5 par # on the merits and impact of codification in this context and for a general analysis of the codification in the South African Companies Act 71 of 2008 and its likely impact and interpretation.

¹¹⁶ Companies Act 71 of 2008 s 7.

¹¹⁷ For a more comprehensive discussion of the role and impact of the social and ethics committee see: Monray M Botha 'Evaluating the Social and Ethics Committee: Is Labour the Missing Link?' (2016) 79(4) *THRHR Reg* 580; S De Lange 'The Social and Ethics Committee in Terms of the 2008 Companies Act: Some

section 72(4) of the legislation, the Minister may prescribe via regulation that a category of companies ‘must each have a social and ethics committee, if it is desirable in the public interest’.¹¹⁸ This must be done having regard to annual turnover, the size of the company’s workforce, or the “nature and extent of the activities of such companies”.¹¹⁹ The social and ethics committee has a broad mandate. Amongst other things, it has the following functions:¹²⁰

- (a) To monitor the company’s activities, having regard to any relevant legislation, other legal requirements or prevailing codes of best practice, with regard to matters relating to

Observations regarding the Exemptions and the Role of the Companies Tribunal’ (2015) 27(3) *SA Merc LJ* 507; Irene-Marie Esser and Piet Delpont P ‘The protection of stakeholders: The South African social and ethics committee and the United Kingdom’s enlightened shareholder value approach: Part 1’ (2017) 50(1) *De Jure* 97; Irene-Marie Esser and Piet Delpont P ‘The protection of stakeholders: The South African social and ethics committee and the United Kingdom’s enlightened shareholder value approach: Part 2’ (2017) 50(2) *De Jure* 221; H J Kloppers ‘Driving Corporate Social Responsibility (CSR) through the Companies Act: An Overview of the Role of the Social and Ethics Committee’ (2013) 16(1) *PELJ* 165; Helena H Stoop ‘Towards Greener Companies – Sustainability and the Social and Ethics Committee’ (2013) 24(3) *Stell LR* 562.

¹¹⁸ Companies Act 71 of 2008 s 72(4)(a). The rest of the section details the fact that it is possible for companies falling within this category to apply for an exemption to the Companies Tribunal. See in this regard: S De Lange ‘The Social and Ethics Committee in Terms of the 2008 Companies Act: Some Observations regarding the Exemptions and the Role of the Companies Tribunal’ (2015) 27(3) *SA Merc LJ* 507.

¹¹⁹ Companies Act 71 of 2008 s 72(4)(a)(i) - (iii). The Regulations to the Act put in place a system to measure the nature and extent of the activities in companies in general. The so-called ‘public interest score’ (see Regulation 26) is used also in instances where it must be determined which accounting standard and financial reporting standards will apply to particular companies (see Section 29(4) and 30(2) and (7) read with regulations 26 - 29). Broadly speaking, the public interest score tallies the number of shareholders, the number of employees, annual turnover and annual third-party liability to arrive at a total ‘score’ representative of the company’s impact to determine the extent to which regulation is required (see Regulation 26). At the moment, the Regulations require all public listed companies to put in place a social and ethics committee as well as any company with a ‘public interest score’ that has in any two of the preceding five years had a ‘public interest score’ exceeding 500 points. This is not an insignificant public interest score and it is likely that only sizeable private companies would be affected.

¹²⁰ Companies Act 71 of 2008 section 72(4) – (10) read with regulation 43.

- (i) social and economic development, including the company's standing in terms of the goals and purposes of -
 - (aa) the 10 principles set out in the United Nations Global Compact Principles;
 - (bb) the OECD recommendations regarding corruptions;
- (ii) good corporate citizenship, including the company's –
 - (aa) promotion of equality, prevention of unfair discrimination, and reduction of corruption;
 - (bb) contribution to development of the communities in which its activities are predominantly conducted...
 - (iii) the environment, health and public safety, including the impact of the company's activities and of its products or services
 - (iv) consumer relationships...
 - (v) labour and employment...
- (b) to draw matters within its mandate to the attention of the Board as occasion requires; and
- (c) to report, through one of its members, to the shareholders at the end of the company's annual general meeting on the matters within its mandate.

This would poise the committee to consider how the company affects a broad number of constituencies and stakeholders and to liaise with and advise the board on these matters. The legislation also mandates that the committee reports back to the shareholders which creates some measure of accountability. Although this is clearly an attempt to encourage companies to focus beyond the immediate interests of shareholders and the financial bottom line, it is hardly an official embrace of stakeholder theory. The matters listed are similar to those that boards of directors in the United Kingdom are required to take account of in terms of section 172 of the 2006

Companies Act, although they are not included in the context of directors' duties but are instead introduced by means of an advisory committee.

5 The Governance codes

Since the first version of the King Code it has been possible to see a more inclusive approach to stakeholder interests. King III was particularly bold in its support for a stakeholder inclusive approach. This is explained in the introduction to King III, which sets out the philosophy of the Report as revolving around 'leadership, sustainability and corporate citizenship.'¹²¹ The introduction highlights that modern governance and leadership are 'characterised by the ethical values of responsibility, accountability, fairness and transparency and based on moral duties that find expression in the concept of Ubuntu.'¹²² In particular strategies and operations should be directed in such a way as to achieve sustainable economic, social and environmental performance. Sustainability is further identified as the 'primary moral and economic imperative of the 21st century' and 'one of the most important sources of both opportunities and risks' that businesses face.¹²³

A particularly interesting outlook, in the South African context, is the report's approach to so-called 'corporate citizenship'. The introduction to King III explained that 'sustainability considerations are rooted in the South African Constitution which is the basic social contract that South Africans have entered into. The Constitution imposes responsibilities upon individuals and juristic persons for the realisation of the most fundamental rights.'¹²⁴ In other words, as everyone has the Constitutional right to, for

¹²¹ King III, Introduction and Background par 8.

¹²² King III, Introduction and Background par 8.

¹²³ King III, Introduction and Background par 8.

¹²⁴ King III, Introduction and Background par 8.

example, a safe and clean environment,¹²⁵ King III contended that a company that pollutes or uses environmentally unsustainable practices is anathema to the principles found in the Constitution. In so doing, it pulls the Constitution squarely into the realm of corporate governance and perhaps even company law. This is of course not revolutionary, as the Constitution is the highest law of the land and in a sense superimposes itself on all legislation as will be considered further in some detail in chapter 5.

Following this, King IV was released on 1 November 2016 and was effective for financial years commencing 1 April 2017.¹²⁶ This most recent version of the South African Code, introduced sweeping changes but did not depart from the core principles or philosophies that shaped the contents of its predecessor. Part 5.1 of the Code is devoted to 'leadership, ethics and corporate citizenship'. Of particular importance for purposes of this analysis, is Principle 3 of part 5.1, which states that '[t]he governing body should ensure that the organisation is and is seen to be a responsible corporate citizen.'¹²⁷ The recommendations that support this principle, emphasise that it is the responsibility of the governing body to 'ensure that the organisation's responsible corporate citizenship efforts include compliance with the Constitution of South Africa (including the Bill of Rights), the law, leading standards, and adherence to its own codes of conduct and policies.'¹²⁸ Oversight and monitoring of the effects of the company's activities and outputs on its status as responsible corporate citizen is recommended on a continuous basis.¹²⁹ Oversight and management in this

¹²⁵ Chapter 2 of the Constitution of the Republic of South Africa, 1996. The principles contained in the Code reiterate the philosophy set out in the introduction and makes clear reference to these departure points. Given that King III has been succeeded by King IV, the rest of this chapter will be devoted to a discussion of the salient points of the latter report and specific examples of principles from the King III Code will not be analysed in greater depth.

¹²⁶ For an overview of developments see: <https://www.iodsa.co.za/page/OurTimeline>

¹²⁷ King IV, Part 5.1: Principle 3.

¹²⁸ Part 5.1, Principle 3: Recommended Practice 12.

¹²⁹ Part 5.1, Principle 3: Recommended Practice 14.

context should take particular account of certain areas, namely the workplace,¹³⁰ the economy,¹³¹ society,¹³² and the environment.¹³³

Part 5.5 of the Code then continues to deal more extensively with stakeholder relationships. Principle 16 underwrites the recommended practices contained in Part 5.5 and states that:

In the execution of its governance role and responsibilities, the governing body should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the organisation over time.

To give effect to this, it is recommended that the governing body exercise ‘ongoing oversight of stakeholder relationship management’ and should oversee that this gives rise to methodologies by means of which stakeholders and stakeholder groupings can be identified – in particular so-called ‘material stakeholders’ based on the extent to which they either effect or are affected by the company’s activities, outputs and outcomes.¹³⁴ It is also recommended that stakeholder risks should be managed as an ‘integral part of organisation-wide risk management’ and that formal mechanisms should be put in place to engage and communicate with stakeholders. Such mechanisms should include the use of dispute resolution mechanisms.¹³⁵ Part 5.5 also recommends certain disclosures relating to stakeholder

¹³⁰ This includes “employment equity; fair remuneration; and the safety, health, dignity and development of employees”. Part 5.1, Principle 3: Recommended Practice 14.

¹³¹ This includes “economic transformation; prevention, detection and response to fraud and corruption; and responsibilities in transparent tax policy.” Part 5.1, Principle 3: Recommended Practice 14.

¹³² This includes “public health and safety; consumer protection; community development; and protection of human rights” Part 5.1, Principle 3: Recommended Practice 14.

¹³³ This includes “responsibilities in respect of pollution and waste disposal; and protection of biodiversity.” Part 5.1, Principle 3: Recommended Practice 14.

¹³⁴ Part 5.5, Recommended Practice 4.

¹³⁵ Part 5.5. Recommended Practice 4.

relationships,¹³⁶ and makes additional recommendations relating to shareholder relationships,¹³⁷ and relationships within groups of companies.¹³⁸

Finally, King IV also makes a number of recommendations in relation to the mandatory Social and Ethics Committee (the SEC) introduced by the 2008 Act. In terms of King IV, the SEC is responsible for oversight of and reporting on responsible corporate citizenship, sustainable development, stakeholder relationships, and organisational ethics.¹³⁹ It also recommends higher standards as far as the composition of the SEC is concerned, suggesting that a majority of the committee should be non-executive directors.¹⁴⁰ Companies not required by law to put in place an SEC, are encouraged to allocate oversight of these matters to a dedicated committee or delegate it to an existing committee.¹⁴¹

The first matter to prominently reference the code, was *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company*,¹⁴² in which the board of a listed public company resigned *en masse* to avoid liability for reckless trading. The company faced multiple court orders in relation to its environmental responsibilities and the directors had been under the impression that it would not be able to meet these requirements and remain financially viable (although the court did not agree that this was an accurate interpretation of the court orders in question).¹⁴³ The case is noteworthy not just for the fact that it makes clear references to the findings of the King Committee on Corporate Governance, but also for the fact that it pertinently

¹³⁶ Part 5.5, Recommended Practice 5.

¹³⁷ Part 5.5, Recommended Practice 6 – 10.

¹³⁸ Part 5.5, Recommended Practice 11 – 19.

¹³⁹ Part 5.3, Recommended practice 68.

¹⁴⁰ Part 5.3, Recommended practice 70.

¹⁴¹ Part 5.3, Recommended practice 68.

¹⁴² *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* 2006 5 SA 333 (W).

¹⁴³ *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* 2006 5 SA 333 (W) at par [14] – [15].

referenced how the demands made by the governance code echoes constitutional imperatives and how this shapes the onus placed on company directors.

As far as the duty to act bona fide in the best interests of the company is concerned, Husain J remained unconvinced that the errant directors had acted 'in good faith upon reasonable grounds for their decision to resign'.¹⁴⁴ As mentioned above, the court concluded that the resignation succeeded only in incapacitating the directors from discharging their duties towards the company, and the court found it unacceptable that they could be allowed to walk away merely because it became convenient to do so. Having accepted appointment as directors of a listed company, they had also accepted the responsibilities that accompany the position. It is at this point that the judge makes the following pivotal observation:¹⁴⁵

Practicing sound corporate governance is essential for the wellbeing of a company and is in the best interests of the growth of this country's economy, especially in attracting new investments. To this end the corporate community within South Africa has widely and almost uniformly accepted the findings and recommendations of the King Committee on Corporate Governance (see King Report on Corporate Governance for South Africa March 2002). Regarding the board of directors the King Report states the following: "The Board is the focal point of the corporate governance system. It is ultimately accountable and responsible for the performance and affairs of the company. Delegating authority to board committees or management does not in any way mitigate or dissipate the discharge by the board and its directors of their duties and responsibility" The conduct of the second to fifth respondents flies in the face of everything recommended in the code of corporate practices and conduct recommended by the King Committee.

¹⁴⁴ *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* 2006 5 SA 333 (W) at par [16.2]

¹⁴⁵ *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* 2006 5 SA 333 (W) at par [16.2]

The court was of the view that the directors had acted irresponsibly in abandoning the listed company of which they were the directors, and that they were themselves guilty of contempt of court, having caused the company to disobey the order despite having knowledge thereof.¹⁴⁶ Notably, the court again referenced the King Committee, this time in the context of the company's social responsibility. It is worth repeating the entire passage:

The King Committee, correctly in my view, stressed that one of the characteristics of good corporate governance is social responsibility. The Committee stated as follows: 'A well-managed company will be aware of, and respond to, social issues, placing a high priority on ethical standards. A good corporate citizen is increasingly seen as one that is non-discriminatory, non-exploitative, and responsible with regard to environmental and human rights issues. A company is likely to experience indirect economic benefits such as improved productivity and corporate reputation by taking those factors into consideration.

The object of the directives is to prevent pollution of valuable water resources. To *permit mining companies and their directors to flout environmental obligations is contrary to the Constitution*, the Mineral Petroleum Development Act and to the National Environmental

¹⁴⁶ The court observed at par [16.8] that '[b]y his act or omission such a director aids and abets the company to be in breach of the order of court against the company. If it were not so a court would have difficulty in ensuring that an order *ad factum praestandum* against a company is enforced by a punitive order.' The judgement cites as authority for this conclusion. *Twentieth Century Fox Film Corporation & others v Playboy Films (Pty) Ltd & another* 1978 (3) SA 202 (W) at 203CD; *Melitka Trading Ltd & others v Commissioner, SARS* 2005 (3) SA 1 (SCA) at paragraph [51] page 19.

Management Act. Unless courts are prepared to assist the State by providing suitable *mechanisms for the enforcement of statutory obligations* an impression will be created that mining companies are free to exploit the mineral resources of the country for profit over the lifetime of the mine, thereafter they may simply walk away from their environmental obligations. This simply cannot be permitted *in a constitutional democracy which recognises the right of all of its citizens to be protected from the effects of pollution and degradation*. For this reason too the second to fifth respondents cannot be permitted to merely walk away from the company conveniently turning their backs on their duties and obligations as directors. I am persuaded that the second to fifth respondents, notwithstanding their sudden resignation, must be held responsible for the first respondent's failure to comply with an order of court.¹⁴⁷

6 Conclusion

Since the earliest decisions considering where the focus of the board should be, opinion has shifted and there has been some evolution in both judicial attitude and the legislative agenda. The so-called 'stakeholder debate' has generated extensive literature. Perhaps one of the most contentious questions in company law has been, and continues to be, the extent to which company directors should take into account stakeholders other than the company's shareholders and if so, which stakeholders in particular. Given the potential impact that a company's activities may have, it is perhaps this second part of the inquiry that is the most vexing of all. It is less contentious to accept that there may be some duty owed to the company's creditors (especially in instances where the company faces financial difficulties). It is

¹⁴⁷ *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* 2006 5 SA 333 (W) at par [16.9]. Emphasis added.

(arguably) a harder case to make, that the directors should take into account other potential stakeholders such as the environment or the communities within which it operates.¹⁴⁸

It is apparent even at face value that the principles and recommendations of King IV make far more onerous demands than the relevant statutory provisions or common law where the directors' responsibilities to act in the company's best interests are concerned. Its (arguably) progressive ethos has certainly not yet been fully embraced by black letter law despite the fact that the legislature had the clear opportunity to do so when drafting the 2008 legislation. Indeed, several of the recommendations contained in King III were included in the 2008 Act. Yet in spite of a general commitment to good governance in the stated purposes contained in section 7 of the 2008 legislation, the legislature chose not to further define the phrase 'best interests of the company', nor did it include the provision similar to section 172 of the UK Companies Act of 2006. This is pertinent as the 2006 Act was already in operation at the time of drafting the 2008 Act, and when subsequent amendments were made to it. It is also clear from the 2008 legislation that statutes of various jurisdictions, including the United Kingdom, were doubtlessly consulted and in some instances incorporated into the South African legislation. The failure to take a more outspoken stance seems then to have been intentional, with the legislature stopping short of imposing a more onerous standard directors where stakeholder interests are concerned.

When interpreting the legislation, one must weigh two competing principles. Firstly, a clear mandate both when interpreting common law and when interpreting statute, that the principles underlying the Constitution should inform all interpretation. On the other, the fact that the purpose of

¹⁴⁸ Although as Du Plessis points out this is becoming increasingly less contentious as the impact on human activities on the environment becomes more difficult to ignore. Du Plessis JJ and Others *Principles of Contemporary Corporate Governance* (4th edn Cambridge UP 2018) 7 – 8.

the legislative provisions in question was apparently not to mandate a pluralist approach to interpretation by the directors of a company.

This chapter provided a broad overview of the viewpoints that informed these debates. It also considered how the existing formal legal regime seems to approach the matter and how this may differ from the approach found in voluntary mechanisms – specifically codes of governance such as King IV and the UK Corporate Governance Code. It seems clear that an interpretation of the director's duty to act in the best interests of the company would require far more from members of company boards, than the current interpretation of the statutory and common law expectations would.

CHAPTER 5

**COLLISIONS AT THE INTERSECTION – PROCEDURAL, PRACTICAL AND
CONSTITUTIONAL CONCERNS**

And the law may be resembled to a nut, which has a shell and a kernel within; the letter of the law represents the shell, and the sense of it the kernel, and as you will be no better for the nut if you make use only of the shell, so you will receive no benefit by the law, if you rely only upon the letter, and as the fruit and profit of the nut lies in the kernel, and not in the shell, so the fruit and profit of the law consists in the sense more than in the letter.¹

1 Introduction

The previous chapters provided an overview of the regulatory environment within which South African companies function, with some references to the position in the United Kingdom and elsewhere. The aim has been to show that, when interpreting company legislation and the common law, there may be room for an approach that considers or even incorporates the principles espoused in voluntary corporate governance codes (specifically South Africa's King IV). As previously argued however, such an approach could face challenges when considered from a constitutional perspective. South African courts are not unique in the sense that their mandate is to state the law, not make it. *Iudicis est ius dicere, non facere*² is perhaps one

¹ *Eyston v. Studd*, 2 Pl. Com. 459, 465 n, 75 Eng. Reprints 688 (C. B. 1574) as quoted by Frederick J. De Sloovere 'Contextual Interpretation of Statutes' (1936) 5(2) *Fordham L.Rev.* 219 at 219.

² Du Plessis LM *Statute Law and Interpretation* in 25(1) *Lawsa* (reissue, 2001) par 367. The author cites numerous examples from the cases recognising the maxim, see for example: *Seluka v Suskin & Salkow* 1912 TPD 258 270; *Harris v Law Society of the Cape of Good Hope* 1917 CPD 449 451; *Union Government (Minister of Mines) v Thompson* 1919 AD 404 425; *Estate Reid v Goodwin* 1920 AD 367 373; *Santy's Wine & Brandy Co (Natal) Ltd v The District Commandant SA Police* 1945 NPD 115 117; *R v Tebetha* 1959 2 All SA 456 (A); 1959 2 SA 337 (A) 346G; *S v Khanyapa* 1979 3 All SA 597 (A); 1979 1 SA 824 (A) 835; *S v Blaauw* 1980

of the first concepts a law student is taught. Many consider it integral to the trias politica doctrine,³ some or other iteration of which is evident in most modern constitutions.⁴ This is also true in the South African Context where the Constitution of the Republic of South Africa, 1996 outlines the distinct functions of the executive, the legislature and the judiciary,⁵ and the Constitutional Court has emphasised that the courts should not overstep these bounds:

[T]he law cannot countenance a situation where, on a case-by-case basis, equity and fairness considerations are invoked to circumvent and subvert the plain meaning of a statutory provision which is rationally connected to the legitimate purpose it seeks to achieve... To do so would be to undermine one of the essential fundamentals of the rule of law, namely the principle of legality.⁶

To say that it is the responsibility of the courts merely to state the law once written, seems a simple thing but of course this is far from the case. The

3 All SA 462 (C); 1980 1 SA 536 (C) 537H; *S v Ncokazi* 1980 3 All SA 83 (Tk); 1980 3 SA 789 (Tk) 797E–F.

³ Also the ‘doctrine of separation of powers’. A comprehensive discussion of the doctrine falls outside of the remit of this thesis but see for example: Charles H Wilson ‘The Separation of Powers under Democracy and Fascism’ (1937) 52(4) *PSQ* 481; Jon D Michaels ‘An Enduring, Evolving Separation of Powers’ (2015) 115(3) *Colum.L.Rev.* 515; Bellamy R ‘The Political Form of the Constitution: the Separation of Powers, Rights and Representative Democracy’ (1996) *JPS* 436.

⁴ Wilson (n3) 481 but cf criticisms of the doctrine highlighted by the author. And see: Holger Ross Lauritsen ‘Democracy and the Separation of Powers: A Rancierean Approach’ (2010) 11(1) *Distinktion* 5, where the author posits an alternative to the hitherto conflicting approaches to *trias politica* as being either “the opposite of democracy (in Marxism) or the essence of democracy (in liberalism)”.

⁵ For an overview of the functioning of the separation of powers doctrine in South African constitutional law see: Stuart Woolman & Michael Bishop (eds) *Constitutional Law of South Africa* (2nd edn Juta, 2014) Revision Service 6 Chapter 12. See also discussion of the relevant provisions etc below. See also *Carmichele v Minister of Safety and Security* (CCT 48/00) [2001] ZACC 22; 2001 (4) SA 938 (CC) at [36] ‘the major engine for law reform is the legislature and not the judiciary’; *Bertie van Zyl (Pty) Ltd and Another v Minister for Safety and Security and Others* (CCT 77/08) [2009] ZACC 11; 2010 (2) SA 181 (CC) at [106] ‘Drafting should be left to the Legislature’.

⁶ *Cool Ideas 1186 CC v Hubbard* 2014 (4) SA474 (CC) at [52].

jurisprudence that informs this area of the law (the interpretation of statutes), and centuries long history of conflicting case law gives some idea of the challenges that confronts a judge when interpreting legal documents generally, and legislation in particular.⁷

Bennion concluded that the ‘essence of statutory interpretation lies in resolving the dichotomy between the ‘pure’ doctrine that the law is to be found in the Act and nowhere else, and the ‘realistic’ doctrine that legislation is an imperfect technique requiring, for the social good, an importation of surrounding information.’⁸ Given that the governance reports in question quite clearly constitute ‘surrounding information’ it is to this dichotomy that the discussion must now turn.

As set out in Chapter 1, the common law duties in question have now been partially codified. However, as the codification is not absolute, the common law will still play an important role even to the extent of constituting a separate cause of action.⁹ As a result, there are two distinct issues of interpretation to consider, namely the interpretation of the statutory duties on the one hand, and on the other the interpretation of the common law duties. As such, the chapter will first discuss the interpretation of the Companies Act 71 of 2008 and following this will turn its attention to the interpretation of the common law duties to the extent not yet considered in chapters 3 and 4 above.¹⁰

⁷ Most recently South Africa’s Supreme Court of Appeal noted that such is the complexity of the debate that even an attempt to conclusively resolve it will in every likelihood prove futile. See *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* (106/2018) [2018] ZASCA 176 at par [60] where Navsa ADP observed that: ‘It is unrealistic to expect of this court or, indeed, of any court, pronouncements that will end theoretical debates that have raged over many decades and settle for all time, terminology that will obviate confusion’.

⁸ FAR Bennion *Bennion on Statutory Interpretation* (3rd ed Butterworths 2002) 520.

⁹ See chapter 1 at text to note 83 and onwards.

¹⁰ It is impossible to engage with the many theories, debates and philosophies that inform this area of the law in a single chapter. It is also outside of the scope of this research to provide a full historic overview. Reference to the history and context of

South African courts currently favour a context driven, purposive approach to interpretation.¹¹ The chapter will provide an overview of the South African position by outlining relevant statutory provisions and considering the theories of interpretation that would apply. A brief summary of the development of the law will be discussed but only to the extent that it highlights the tensions that arise when interpreting legislative texts. Following this, the impact of the Constitution of the Republic of South Africa, 1996 on the interpretation of the Act will be considered. The chapter concludes with a discussion of the interpretation and development of the common law.

2 From Text to Context

a. Relevant Developments in the Law of the Interpretation of Documents

As is the case with most legal subjects, the law governing statutory interpretation encompasses numerous theories¹² and has generated extensive debate.¹³ The most common or conventional theories include

the law relating to the interpretation of statutes more generally will be considered only in overview to the extent appropriate for purposes of this research.

¹¹ See for example *Standard Bank Investment Corporation v The Competition Commission and Others* [2000] 2 All SA 245 (A), 2000 (2) SA 797 (SCA) at par [21]; *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) SA 593 (SCA).

¹² Apart from those discussed below there are, for example, also the objectivism and the judicial or free theories. See Du Plessis (n2) 317 – 318.

¹³ See in general: Lourens Du Plessis *Re-Interpretation of Statutes* (Durban: Butterworths 2002); GE Devenish *Interpretation of Statutes* (Juta 1992); Rupert Cross, John Bell and Sir George Engle *Statutory Interpretation* (Butterworths 1995); Bennion (n8); Lord Justice Sales 'Modern Statutory Interpretation' (2017) 38(2) *Stat.L.R* 125.

literalism,¹⁴ intentionalism,¹⁵ and purposivism.¹⁶ The Companies Act 71 of 2008 clearly favours a purposive method of interpretation,¹⁷ and what could perhaps be called a contextual approach taking account of purpose was most recently endorsed by the Supreme Court of Appeal¹⁸ and the

¹⁴ Du Plessis explains that “[a]ccording to literalism in its crude, unqualified form, the meaning of a statutory provision can (and must) be retrieved from the *ipsissima verba* in which it is couched, regardless of manifestly unjust or even absurd consequences. Legislative authority is unquestioningly deferred to and no one dare tamper with the very words that the legislature used to express its will.” Du Plessis (n2) 314. Although such an unqualified form of literalism is “on the wane” (see also Devenish (n13) 26). Du Plessis points out that adapted and amplified versions of the theory remain ‘alive and kicking’ and that other approaches to statutory interpretation ‘are regarded as deviations from literalism instead of theoretical positions in their own right.’ Du Plessis (n2) 314.

¹⁵ The theory contends that the paramount rule of statutory interpretation is that the real intention of the legislature, once discerned, must be given effect to. See for example: Steyn, LC *Uitleg van Wette* (5 ed Juta 1981) at 2; Devenish, GE *Interpretation of Statutes* (Juta 1992) at 33. Wallis JA on behalf of the Supreme Court of Appeal in the judgement of *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) recently criticised and rejected this approach in favour of a purposive method to interpretation. The court considered the prevailing criticisms and debates, referring *inter alia* to the work of ... and case law from the United Kingdom and Australia. An overview of this analysis falls outside of the scope of this chapter. See however *Natal Joint Municipal Pension Fund v Endumeni Municipality* at par [20] – [23] and the sources there cited.

¹⁶ Purposive analysis is a widely accepted modern approach, and can be described along the following lines: “To achieve a sound interpretation of a legislative text, interpreters must identify and take into account the purpose of the legislation, this includes the purpose of the provision to be interpreted as well as larger units – parts, divisions, and the Act as a whole. Once identified, the purpose is relied on to help establish the meaning of the text. It is used as a standard against which proposed interpretations are tested: an interpretation that promotes the purpose is preferred over one that does not, while interpretations that would tend to defeat the purpose are avoided.” Ruth Sullivan *Statutory Interpretation* (2ed Irwin Law Inc 2007) 194.

¹⁷ See section 5 & section 7.

¹⁸ The decision has been cited and followed by both the Supreme Court of Appeal and the Constitutional Court; most recently in *Municipal Employees Pension Fund v Natal Joint Municipal Pension Fund (Superannuation) and Others* 2018 (2) BCLR 157 (CC) ((2018) 39 ILJ 311; [2017] ZACC 43) par [28]; *Trinity Asset Management (Pty) Ltd v Grindstone Investments 132 (Pty) Ltd* 2018 (1) SA 94 (CC) (2017 (12) BCLR 1562; [2017] ZACC 32) par [52] and *National Police Commissioner and Another v Ngobeni* 327/2017 [2018] ZASCA 14; 2018 (4) SA 99 (SCA) at par [] amongst others.

remainder of this overview will focus only on the current law and those developments that directly informed it.¹⁹

In South African law, the primary rule in the construction of statutory provisions had long been to ascertain the intention of the Legislature.²⁰ So well-known was this so-called ‘golden rule’ of interpretation, that it was considered trite.²¹ Ascertaining the intention of the Legislature was achieved ‘in the first instance, by giving the words of the provision under consideration the ordinary grammatical meaning which their context dictates, unless to do so would lead to an absurdity so glaring that the [Legislature] could not have contemplated it.’²²

The courts gradually began to acknowledge that words used in a statute are to be interpreted in the light of their context and that the context in this sense should not be limited to the rest of the statute but should include its scope and purpose and within limits, also its background. These developments primarily came about following a seminal minority judgement by Schreiner JA in the case of *Jaga v Dönges NO & Another; Bhana v Dönges*

¹⁹ Other theories of interpretation include objectivism, linguistic turn and value based approaches. See JL Yeats (ed) *Commentary on the Companies Act of 2008* (Juta 2018) 1-36.

²⁰ *Manyasha v Minister of Law and Order* 1999 (2) SA 179 (SCA) at 185, neutral citation page 8; *Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School* (207/07) [2008] ZASCA 70 (30 May 2008) at par 16. See for example the following cases where the phrase ‘the intention of the Legislature’ was used: *Ebrahim v Minister of the Interior* 1977 (1) SA 665 (A) at 677-678; *Protective Mining & Industrial Equipment Systems (Pty) Ltd (formerly Hampo Systems (Pty) Ltd) v Audiolens (Cape) (Pty) Ltd* 1987 (2) SA 961 (A) at 991; *Summit Industrial Corporation v Claimants against the Fund Comprising the Proceeds of the Sale of the MV Jade Transporter* 1987 (2) SA 583 (A) at 596 – 597, and *Manyasha v Minister of Law and Order* 1992 (2) SA 179 (SCA) at 185 B-C. The use of this ‘slippery phrase’ (as it was referred to by Lord Watson in the famous case of *Salomon v A Salomon & Co Ltd* (1987) AC 22 at 38) was strongly criticised in the influential judgement of *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA), considered at greater length below.

²¹ *Manyasha v Minister of Law and Order* 1999 (2) SA 179 (SCA) at 185, neutral citation page 8.

²² *Manyasha v Minister of Law and Order* 1999 (2) SA 179 (SCA) at 185, neutral citation page 8.

*NO & Another*²³ in which he was of the now famous opinion that ‘the legitimate field of interpretation should not be restricted as a result of an excessive peering at the language to be interpreted without sufficient attention to the contextual scene.’²⁴ As early as 2004 the Constitutional Court described the ‘emerging trend’ in statutory interpretation as having ‘regard to the context in which the words occur, even where the words to be construed are clear and unambiguous.’²⁵ In other words, context was to become more than a mere afterthought to be considered only in the final instance when the wording defied an immediately apparent interpretation.

One must consider these developments against the backdrop of South African case law that has long recognised that the aim of statutory interpretation is also ‘to give effect to the object or purpose of the legislation in question’.²⁶ Purposivism attaches meaning in light of the purpose that a particular provision aims to achieve given the context of the

²³ *Jaga v Dönges NO & Another; Bhana v Dönges NO & Another* 1950 (4) SA 653 (A).

²⁴ *Jaga v Dönges NO & Another; Bhana v Dönges NO & Another* 1950 (4) SA 653 (A) at 662G-H and 664H. These words of Schreiner JA (from the dissenting judgement) have been described as a “seminal exposition of an interpretative *modus operandi* honouring the exigencies of both language and context” and “one of the most frequently relied on minority judgments in the history of South African case law.” See Du Plessis (n2) par 310. The relevant dictum has since been quoted with approval by the Constitutional Court: *Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs & Others* (CCT 27/03) [2004] ZACC 15 (12 March 2004) para 89. And see: *Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School* (207/07) [2008] ZASCA 70 (30 May 2008) at par 17 where the Supreme Court of Appeal cites the judgement with approval.

²⁵ *Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs & Others* (CCT 27/03) [2004] ZACC 15 (12 March 2004) para 90. In reaching this conclusion the court referred to *Thoroughbred Breeders’ Association v Price Waterhouse* (416/99) [2001] ZASCA 82; [2001] 4 All SA 161 (A) (1 June 2001) at par 12 of the concurring judgement where the court concludes that ‘The days are long past when blinkered peering at an isolated provision in a statute was thought to be the only legitimate technique in interpreting it if it seemed on the face of it to have a readily discernible meaning.’ And see: *University of Cape Town v Cape Bar Council* (100/86) [1986] ZASCA 86 (4 September 1986) page 18; 1986 (4) SA 903 (A) at 941D-E

²⁶ *Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School* (207/07) [2008] ZASCA 70 (30 May 2008) at par 19; *Standard Bank Investment Corporation v The Competition Commission and Others* 44/2000, 50/2000) [2000] ZASCA 20 at par [16].

document as a whole.²⁷ The approach was summarised famously by Innes J in the judgement of *Dadoo Ltd and Others v Krugersdorp Municipal Council*:

28

Speaking generally, every statute embodies some policy or is designed to carry out some object. When the language employed *admits of doubt*, it falls to be interpreted by the court according to recognised rules of construction, paying regard, in the first place, to the ordinary meaning of the words used, but departing from such meaning under certain circumstances, if satisfied that such departure would give effect to the policy and object contemplated...But there must, of course, be a limit to such departure. A Judge has authority to interpret, but not to legislate, and he cannot do violence to the language of the lawgiver by placing upon it a meaning of which it is not reasonably capable, in order to give effect to what he may think to be the policy or object of the particular measure.

The above, oft cited judgement of Innes CJ in *Dadoo* was recently referred to in *L D v Technology Corporate Management (Pty) Ltd and Others; S D v L D*,²⁹ and *Smyth v Investec Bank Ltd*³⁰ where the SCA again emphasised ‘that it would be wrong for courts to ignore the clear language of a statute under the guise of adopting a purposive interpretation as doing so would be straying into the domain of the legislature.’³¹ Although the passage from *Dadoo*’s case therefore illustrates the courts’ willingness to consider the object or purpose of legislation, Schutz JA pointed out in the *Standard Bank*

²⁷ See above at note 20. And see: Du Plessis (n2) 316. This purpose is determined (in terms of the classical version of purposivism) by means of the so-called ‘mischief rule’ which contends that the purpose of enacted law is to ‘suppress mischief’. The rule, taken from *Heydon’s case* (1584) 3 Co Rep 7a 7b, predates literalism and stems from an era where purposive interpretation was a practical necessity due to the fact that ‘judicial rectification and augmentation of fragmentary statutes was inevitable at the time...because Parliament met irregularly.’.

²⁸ 1920 AD 530 at 543.

²⁹ (40036/16; 35926/16) [2018] ZAGPJHC 69 (23 February 2018) par [65] and [66].

³⁰ 2015 JDR 2278 (GP) par [64]. Subsequently confirmed on appeal: 2018 (1) SA 494 (SCA) par [45].

³¹ [2018] 1 All SA 1 (SCA), 2018 (1) SA 494 (SCA) par [45].

case that the passage also ‘reflects that it is not the function of a court to do violence to the language of a statute and impose its view of what the policy or object of a measure should be.’³²

The court reiterated that one is confronted by ‘the ultimate logical dilemma’ if one were to subvert the words chosen by Parliament in favour of the spirit of the law and referred again the judgement in *Dadoo’s case*³³ where Innes CJ considered the meaning of authorities contending that an action which does not contravene the language of a piece of legislation may nonetheless infringe its spirit and as such be invalid.³⁴

In considering this, Schultz JA dismissed the appellant’s contention that the semantic or literalist approach enjoyed dwindling support in modern legal theory. The court pointed out that s 43 of the Constitution vests the legislative authority of the national sphere of government in parliament and this authority is exercised mainly by enacting legislation.³⁵ These pieces of legislation are expressed in words and as such, interpretation ‘concerns the meaning of the words used by the Legislature and it is therefore useful to approach the task by referring to the words used, and to leave extraneous considerations for later’ as Harms JA contended in *Abrahamse v East London Municipality and Another; East London Municipality v Abrahamse*.³⁶

³² *Standard Bank Investment Corporation v The Competition Commission and Others* [2000] 2 All SA 245 (A), 2000 (2) SA 797 (SCA) at par [16]. Schultz JA cites the very famous dictum from the judgement of *Jaga v Dönges NO and Another; Bhana v Dönges NO and Another* 1950 (4) SA 653 (A) where Shreiner JA warns of the dangers of a purposive approach being used to justify a disregard for the actual text (at 664).

³³ *Dadoo Ltd and Others v D Krugersdorp Municipal Council* 1920 AD 530 at 543.

³⁴ *Dadoo Ltd and Others v D Krugersdorp Municipal Council* 1920 AD 530 at 543.’

³⁵ *Standard Bank Investment Corporation v The Competition Commission and Others* [2000] 2 All SA 245 (A), 2000 (2) SA 797 (SCA) at par [21].

³⁶ *Abrahamse v East London Municipality and Another; East London Municipality v Abrahamse* 1997 (4) SA 613 (SCA) at 632.

Although Schultz JA went on to iterate that this does not imply that South African law is not an ‘enthusiastic supporter of ‘purposive construction’,³⁷ he endorsed a more reticent approach and appears to emphasise that the purpose is only to be considered once the application of the ‘literal interpretation principle’ results in ambiguity and one seeks to determine which of more than one meaning might have been intended by the legislature.³⁸

Although the court in *Standard Bank* referenced the revolutionary judgement of Schreiner JA in *Jaga v Dönges NO and Another; Bhana v Dönges NO and Another* to illustrate the interaction between text and context, no mention was made of the fact that Schreiner JA in that matter in fact suggested that there could be two approaches to interpretation. Either one may split the inquiry into two parts, concentrating firstly on whether the language in question appears to have one clear ordinary meaning (in which case one would, confine the consideration of context ‘only to cases where the language appears to admit of more than one meaning’).³⁹ Alternatively, one may from the beginning ‘consider the context and the language to be interpreted together.’⁴⁰

Nearly a decade later, in a seminal decision the Supreme Court of Appeal in *Natal Joint Municipal Pension Fund v Endumeni Municipality* (hereafter

³⁷ *Standard Bank Investment Corporation v The Competition Commission and Others* [2000] 2 All SA 245 (A), 2000 (2) SA 797 (SCA) at par [21].

³⁸ *Standard Bank Investment Corporation v The Competition Commission and Others* [2000] 2 All SA 245 (A), 2000 (2) SA 797 (SCA) at par [21]. Schultz JA endorses the approach to purposivism set out by Smalberger JA in the judgement of *Public Carriers Association and Others v Toll Road Concessionaries (Pty) Ltd and Others*(323/89) [1989] ZASCA 164 (30 November 1989) page 16, 1990 (1) SA 925 (A) at 942I-944A.

³⁹ *Jaga v Dönges NO and Another; Bhana v Dönges NO and Another* 1950 (4) SA 653 (A) at 662.

⁴⁰ *Jaga v Dönges NO and Another; Bhana v Dönges NO and Another* 1950 (4) SA 653 (A) at 663.

Endumeni)⁴¹ gave South African courts the unambiguous mandate to apply the ‘second of the two possible approaches followed by Schreiner JA in *Jaga v Donges NO and Another*’, namely that one should from the outset consider the context and the language together, with neither predominating over the other.⁴² In a judgement written on behalf of the majority Wallis JA in no uncertain terms, rejected the ubiquitous golden rule of interpretation⁴³ or any form of intentionalism and embraced a shift from text to context in the law relating to the interpretation of documents which manifested itself over the last century,⁴⁴ and which was confirmed by the Constitutional Court as

⁴¹ (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA). The decision has been cited and followed by both the Supreme Court of Appeal and the Constitutional Court; most recently in *Municipal Employees Pension Fund v Natal Joint Municipal Pension Fund (Superannuation) and Others* 2018 (2) BCLR 157 (CC) ((2018) 39 ILJ 311; [2017] ZACC 43) par [28]; *Trinity Asset Management (Pty) Ltd v Grindstone Investments 132 (Pty) Ltd* 2018 (1) SA 94 (CC) (2017 (12) BCLR 1562; [2017] ZACC 32) par [52] and *National Police Commissioner and Another v Ngobeni* 327/2017 [2018] ZASCA 14; 2018 (4) SA 99 (SCA) at par [] amongst others.

⁴² *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [19].

⁴³ Wallis JA considers the notion that interpretation is aimed at establishing the ‘intention of the Legislature’ and concludes that, despite it being a phrase used by generations of lawyers, it is unhelpful. It is namely nearly impossible to discern the meaning that Parliament may or may not have attributed to a legislative provision in a context of which they may only be dimly aware – if indeed it is a context that they contemplated at all. The motivations of lawmakers when passing legislation are manifold and in many circumstances, it is entirely artificial to speak of the intention of parliament and that ‘to characterise the task of interpretation as a search for such an ephemeral and possibly chimerical meaning is unrealistic and misleading.’: *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [20] – [21].

⁴⁴ *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [18]. Indeed, a good eight years before the judgement, Ngcobo J described himself as ‘troubled’ by an approach which ‘pays too much attention to the ordinary language of the words’ and by doing so ‘ignores the colour given to the language by the context’ see *Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs & Others* (CCT 27/03) [2004] ZACC 15 (12 March 2004) at par [92]. The court quotes from the decision of the Supreme Court of Appeal in *Thoroughbred Breeders’ Association v Price Waterhouse* (416/99) [2001] ZASCA 82; [2001] 4 All SA 161 (A) (1 June 2001) at par [12] of the concurring judgment.

an ‘emerging trend in statutory construction’⁴⁵ and a Constitutional requirement.

The court emphasised again that the ‘sole benefit of expressions such as “the intention of the legislature” ... is to serve as a warning to courts that the task they are engaged upon is discerning the meaning of words used by others, not one of imposing their own views of what it would have been sensible for those others to say’.⁴⁶ The proper approach is ‘*from the outset* to read the words used in the context of the document as a whole and in the light of all relevant circumstances.’⁴⁷ In resolving any ambiguity that may arise, the court mentioned specifically that the apparent purpose of the provision and the context in which it occurs will be important guides to correct interpretation, and that ‘[a]n interpretation will not be given that leads to impractical, unbusinesslike or oppressive consequences or that will stultify the broader operation of the legislation or contract under consideration.’⁴⁸

The ratio is worth repeating here in full:

The present state of the law can be expressed as follows. Interpretation is the process of attributing meaning to the words used in a document, be it legislation, some other statutory instrument, or contract, having regard to

⁴⁵ *Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs & Others* (CCT 27/03) [2004] ZACC 15 (12 March 2004) at par [90]. The court in *Endumeni* referred also to the following comment made by Sir Anthony Mason CJ in the judgement of *Rainy Sky SA and others v Kookmin Bank* [2011] UKSC 50; [2012] Lloyds Rep 34 (SC) at par [21]: “Problems of legal interpretation are not solved satisfactorily by ritual incantations which emphasise the clarity of meaning which words have when viewed in isolation, divorced from their context. The modern approach to interpretation insists that context be considered in the first instance, especially in the case of general words, and not merely at some later stage when ambiguity might be thought to arise.”

⁴⁶ *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [24].

⁴⁷ *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [24].

⁴⁸ *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [24].

the context provided by reading the particular provision or provisions in the light of *the document as a whole and the circumstances attendant upon its coming into existence*. Whatever the nature of the document, consideration must be given to the language used in the light of the *ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose to which it is directed and the material known to those responsible for its production*. Where more than one meaning is possible each possibility must be weighed *in the light of all these factors*. The process is objective not subjective. A sensible meaning is to be preferred to one that leads to insensible or unbusinesslike results or undermines the apparent purpose of the document. Judges must be alert to, and guard against, the temptation to substitute what they regard as reasonable, sensible or businesslike for the words actually used. To do so in regard to a statute or statutory instrument is to cross the divide between interpretation and legislation. In a contractual context it is to make a contract for the parties other than the one they in fact made. The ‘inevitable point of departure is the language of the provision itself’, read in context and having regard to the purpose *in the light of all these factors*. The process is objective not subjective.⁴⁹

In spite of a clear preference for an approach which embraces context from the outset, the judgement should not be interpreted to suggest that the text has become an afterthought: the court in *Endumeni* emphasised the divide between interpretation and legislation and in so doing echoed other judgements that have urged the courts not to allow a purposive approach to interpretation to undermine the actual words written.⁵⁰

⁴⁹ *Natal Joint Municipal Pension Fund v Endumeni Municipality* (920/2010) [2012] ZASCA 13 (15 March 2012) 2012 (4) SA 593 (SCA) at par [18].

⁵⁰ See for example *In re former Highlands Residents: Sonny v Department of Land Affairs* 2000 (2) SA 351 (LCC) at par [12] where the South African Land Claims Court remarks: “Important as the purpose of legislation may be, elevating it to the prevailing factor of interpretation will not, in my view, always provide the key to unlock meaning.”

Although it introduced an about-turn in the courts' approach to statutory interpretation in South African law, *Endumeni* was not entirely clear on exactly what its impact should be. The '*context in which the provision appears*' seems a clear reference to the textual context or in other words the entirety of the statute. However, the judgement does not indicate what is meant by '*the apparent purpose to which it is directed and the material known to those responsible for its production*'. Clearly, if broadly construed this could allow a great deal of material indeed. That this may be the result, appeared from the subsequent judgement of *Bothma-Bato Transport (Edms) Bpk v S Bothma & Seun Transport (Edms) Bpk*⁵¹ where Wallis JA reiterated that:

Whilst the starting point remains the words of the document, which are the only relevant medium through which the parties have expressed their contractual intentions, the process of interpretation does not stop at a perceived literal meaning of those words, but considers them *in the light of all relevant and admissible context*, including the *circumstances in which the document came into being*. The former distinction between *permissible background and surrounding circumstances, never very clear, has fallen away*. Interpretation is no longer a process that occurs in stages but is 'essentially one unitary exercise'. Accordingly it is no longer helpful to refer to the earlier approach.

The court here mentioned specifically that it is the 'admissible context' that is to be considered. This could be interpreted as narrowing the scope of *Endumeni* and confirming that what is implied by context is all surrounding circumstances subject to admissibility in terms of the existing law. The change being introduced by *Endumeni* then, has to do almost exclusively with how context is to be applied and not with what that context comprises of. However, the very same sentence then iterates (without qualifying) that 'relevant and admissible context' *includes* 'the circumstances in which the

⁵¹ *Bothma-Bato Transport (Edms) Bpk v S Bothma & Seun Transport (Edms) Bpk* [2013] ZASCA 176 [12].

document came into being' and does away with 'the former distinction between permissible background and surrounding circumstances'. This could be construed as an even bolder change, one which disregards the rules that have hitherto excluded large swathes of extra-textual material from the interpretive process.⁵²

As mentioned, the courts embraced *Endumeni* in a chorus and it is cited almost as a matter of course whenever any statute or contract faces judicial scrutiny. However, it is perhaps because of this vagueness that *Endumeni* is often given lip service only and in fact has seemingly been used as authority for anything under the sun. The following cogent summary by Perumalsamy illustrates this point:⁵³

In a growing number of judgments that cite *Endumeni*, it seems that it is often only cited for the proposition that it is the correct approach to the interpretation of statutes, wills and contracts. But immediately after this, our Courts revert to the ordinary meaning as it was intended by the legislature or contracting parties, doing the exact opposite of *Endumeni*. In addition to this, even though *Endumeni*, was decided in 2012, and first endorsed by the Constitutional Court in 2013, (See in particular *KwaZulu Natal Joint Liaison Committee v MEC Department of Education, KwaZulu Natal* 2013 (4) SA 262 (CC) [128]; *National Credit Regulator v Opperman* 2013 (2) SA 1 (CC) [96].) in a number of decisions, the Constitutional Court, Supreme Court of Appeal and some divisions of the High Court have both endorsed *Endumeni* and the old approach to statutory interpretation simultaneously without recognising the contradiction.⁵⁴

⁵² Rightly or wrongly so.

⁵³ Kessler Perumalsamy 'The Life and Times of Textualism in South Africa' (2019) *PELJ* 10 (original footnotes appear in brackets).

⁵⁴ The author cites a number of examples that illustrate the point: *Trinity Asset Management (Pty) Ltd v Grindstone Investments 132 (Pty) Ltd* 2018 (1) SA 94 (CC) [52]; *Reezen Ltd v Excellerate Holdings Ltd* [2018] ZAGPJHC 409 [43-44]; *Public Servants Association v Head of Department of Health, Gauteng and Others* 2018 (2) SA 365 (CC) [43]; *Jordaan and Another v Tshwane City and Another and Four Similar Cases* 2017 (2) SA 295 (GP) [69]; *Tshwane City v Mitchell* 2016 (3) SA 231 (SCA); *S v*

It appears from this that Wallis JA's funeral for the old approach⁵⁵ was not as well attended by the South African judiciary as the learned judge may have hoped. Perumalsamy predicted that, the ultimate outcome will likely be that subsequent decisions of the Supreme Court of Appeal will give further structure to the decision reached in *Endumeni*. Indeed, he pointed to the first judgement to question the absolute wisdom of *Endumeni* – a dissenting opinion of Majiedt JA and Davis AJA in the case of *CSARS v Daikin Air Conditioning South Africa*.⁵⁶

The recent decision by the Supreme Court of Appeal in *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association*⁵⁷ seems finally to have vindicated Perumalsamy's prediction. Navsa ADP strongly criticized the South African courts' treatment of the principles set out in *Endumeni*. Yet again the judgement confirms that the Supreme Court of Appeal 'has consistently stated that in the interpretation exercise the point of departure is the language of the document in question. Without the written text there would be no interpretive exercise. In cases of this nature, the written text is what is presented as the basis for a justiciable issue.... As a matter of policy, courts have chosen to keep the admission of evidence within manageable bounds.'⁵⁸

Navsa ADP laments the fact that the SCA has seen 'too many cases of extensive, inconclusive and inadmissible evidence being led' and that this

Nteta and Others 2016 (2) SACR 641 (WCC); *AfriForum and Another v University of the Free State* 2018 (2) SA 185 (CC) [43]'.

⁵⁵ See *Bothma-Bato Transport (Edms) Bpk v S Bothma & Seun Transport* [2013] ZASCA 176 at par [12] quoted above where Wallis JA professes that "it is no longer helpful to refer to the old approach."

⁵⁶ *CSARS v Daikin Air Conditioning South Africa (Pty) Ltd* [2018] ZASCA 66.

⁵⁷ *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* 2019 (3) SA 398 (SCA).

⁵⁸ *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* 2019 (3) SA 398 (SCA) [63].

trend seems to be on the increase.⁵⁹ Decrying the fact that the pendulum has swung too far, the court called for a return to the foundational principles relating to the extent of evidence led in relation to written texts as set out by the SCA in *KPMG Chartered Accountants (SA) v Securefin Ltd & another*⁶⁰ where the court confirmed that the parol evidence rule remained part of South African law, that ‘interpretation is a matter of law and not of fact and, accordingly interpretation is a matter for the court and not for witnesses ... [and that] the rules about admissibility of evidence in this regard do not depend on the nature of the document, whether statute, contract or patent.’⁶¹

Importantly, the Court in *KPMG* confirmed that ‘to the extent that evidence may be admissible to contextualise the document (since “context is everything”) to establish its factual matrix or purpose or for purposes of identification, “one must use it as conservatively as possible”(*Delmas Milling Co Ltd v Du Plessis* 1955 (3) SA 447 (A) at 455B-C).’⁶² The court unreservedly endorses this approach, as Navsa ADP observes:

In *KPMG* this court, as we are now, was expressing judicial frustration at how hitherto recognised inadmissible evidence, which, in any event, is invariably inconclusive, was being led in support of a party’s contentions in relation to written text ... Before us it was not suggested that the foundational principles set out in *KPMG* no longer apply or should be abandoned. Nor is such a suggestion sustainable. Those principles continue to be applicable. *Endumeni*, ... reaffirmed those principles and did not detract from them.⁶³

⁵⁹ *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* 2019 (3) SA 398 (SCA) [63].

⁶⁰ [2009] ZASCA 7; 2009 (4) SA 399 (SCA).

⁶¹ [2009] ZASCA 7; 2009 (4) SA 399 (SCA) at [39].

⁶² [2009] ZASCA 7; 2009 (4) SA 399 (SCA) at [39]. Original reference included in brackets.

⁶³ *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* 2019 (3) SA 398 (SCA) [68] – [69].

These dissenting voices are of course a far cry from a return to the 'golden rule' or intentionalism, and probably remains uncontentious to say that South African law seems indeed to have fully embraced a context driven approach to the interpretation of legal documents. What this discussion hopes to show however, is that the parameters of this context remain vague. It is therefore conceivable that a court might justify turning to a report such as King IV as an interpretive aide, especially given that the Department of Trade and Industry cites its predecessor on numerous occasions in the policy paper that informed the drafting process,⁶⁴ and the Act thought not referencing King III by name, refers clearly to good corporate governance as one of its purposes in section 7.⁶⁵

Yet, the emphatic emphasis of the most recent decision is unambiguous in its warning that extra-textual evidence should be treated with caution and admitted only in the rarest of cases. Any potential floodgates that *Endumeni* might temporarily have opened are apparently fast closing. It bears mention that the decision in *Blair Atholl* had to do with the interpretation of a contract and not statute and as such some of the court's remarks may be considered as having been made in obiter. That being said, the judgement in *KPMG* that Navsa ADP relies upon specifically points out that it does not make any difference which legal text one is interpreting as far as this reticence towards extra-textual material is concerned.

In conclusion, having considered the relevant case law, it appears possible but unlikely that a court will allow evidence related to the governance

⁶⁴ *South African Company Law for the 21st Century – Guidelines for Corporate Law Reform* Government Gazette 26493 of 23 June 2004 available online at https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf.

⁶⁴South African Company Law for the 21st Century – Guidelines for Corporate Law Reform at 11.

⁶⁵See below at note 150.

codes to inform the provision of the statute. For the moment the analysis must now turn to a further reality of statutory interpretation in the South African context that may give indirect impetus to an appeal to King IV when interpreting the Companies Act – a Constitution that permeates all law.

b. Corporate Law Through the Prism of the Bill of Rights

An end to Apartheid heralded a new era in South Africa and the adoption of a codified constitution. The supremacy of the constitution is enshrined in chapter one as a founding provision which states: ‘This Constitution is the supreme law of the Republic; law or conduct inconsistent with it is invalid, and the obligations imposed by it must be fulfilled.’⁶⁶

For purposes of this discussion, one of the most important provisions, is Section 39 of the Constitution, which deals with the interpretation of the Bill of Rights.⁶⁷ It gives the courts a specific mandate ‘when interpreting any legislation, and when developing the common law or customary law’, namely that every court, tribunal or forum must ‘promote the spirit, purport and objects of the Bill of Rights.’⁶⁸ Of course, this imperative applies not only to corporate law, and as Langa DP concluded, ‘[t]his means that all statutes must be interpreted through the prism of the Bill of Rights. All law-making authority must be exercised in accordance with the Constitution...The

⁶⁶Section 2, Constitution of the Republic of South Africa, 1996.

⁶⁷ It must be made clear at the outset that it is impossible to do justice to the debates, discourse and numerous cases that inform the impact of the constitution on statutory interpretation in the South African context, nor is this required for the analysis at hand. The overview provided here highlights the most salient points that pertain directly to the research question. Numerous comprehensive publications deal with the matter in detail. See for example:

⁶⁸ Section 39(2). Subsection 39(3) toes on to state that “[t]he Bill of Rights does not deny the existence of any other rights or freedoms that are recognised or conferred by common law, customary law or legislation, to the extent that they are consistent with the Bill”.

Constitution requires that judicial officers read legislation, where possible, in ways which give effect to its fundamental values'.⁶⁹

The Bill of Rights is contained in Chapter 2 of the Constitution, where it is described as 'a cornerstone of democracy in South Africa.' The Bill of Rights 'enshrines the rights of all people' and 'affirms the democratic values of human dignity, equality and freedom'.⁷⁰ Its universal application is again reiterated in section 8 which confirms that '[t]he Bill of Rights applies to all law, and binds the legislature, the executive, the judiciary and all organs of state'.⁷¹ Its provisions will bind a natural or juristic person 'if, and to the extent that, it is applicable, taking into account the nature of the right and the nature of any duty imposed by the right'.⁷² Finally, when applying a

⁶⁹ *Hyundai case: Investigating Directorate: Serious Economic Offences and Others v Hyundai Motor Distributors (Pty) Ltd and Others* 2001 (1) SA 545 (CC) at 558 par [21]. The approach is summarised as follows by the Land Claims Court *In re Former Highlands Residents: Sonny v Department of Land Affairs* 2000 (2) SA 351 (LCC) at par [10] in relation to the interpretation of the Restitution of Land Rights Act 22 of 1994: "The Court must exercise its powers to order restitution within the confines of the Restitution Act, duly interpreted by using all relevant norms of interpretation (the presumptions and other intra-textual and extra-textual aids). Where the language of a statute leaves a gap to be filled, the Court must fill the gap. In doing so, it must reconstruct the thinking contained in the statute, consider the practical implications and come up with a solution which conforms with the purpose of the statute and with the spirit, purport and objects of the Bill of Rights, while also serving the requirements of justice and equity."

⁷⁰ Section 7(1), Constitution of the Republic of South Africa, 1996. Section 7 further iterates that the state must "respect, protect, promote and fulfil the rights in the Bill of Rights (s 7(2)), and sets out when the rights contained therein may legitimately be limited (s 7(3)).

⁷¹ Section 8(1), Constitution of the Republic of South Africa, 1996.

⁷² Section 8(2), Constitution of the Republic of South Africa, 1996. Ss 8(4) further states that: "A juristic person is entitled to the rights in the Bill of Rights to the extent required by the nature of the rights and the nature of that juristic person." The courts have since interpreted this provision to confer rights of privacy, property and expression on juristic persons. See for example regarding the right to freedom of expression enjoyed by the press: *Khumalo v Holomisa* 2002 (5) SA 401 (CC), 2002 (8) BCLR 771 (CC); *Sayed v Editor, Cape Times* 2004 (1) SA 58, 62–63 (C). Although naturally juristic persons could not benefit from all rights, see for example *Investigating Directorate: Serious Economic Offences & Others v Hyundai Motor Distributors (Pty) Ltd & Others: In re Hyundai Motor Distributors (Pty) Ltd & Others v Smit NO & Others* 2001 (1) SA 545 (CC), 2000 (10) BCLR 1079 (CC) ('Hyundai') regarding the right to human dignity. And see in general: Woolman and Bishop (eds) (n5) ch31 – p39.

provision of the Bill of Rights to a natural or juristic person a court 'must apply, or if necessary develop, the common law to the extent that legislation does not give effect to that right.'⁷³

Chapter 8 of the Constitution is devoted to the courts and the administration of justice. Section 165 vests judicial authority of the republic in the courts,⁷⁴ and confirms their independence, 'subject only to the Constitution and the law, which they must apply impartially and without fear, favour or prejudice'.⁷⁵ Section 173 confers on the Constitutional Court, the Supreme Court of Appeal and the High Court of South Africa the 'inherent power to protect and regulate their own process, *and to develop the common law, taking into account the interests of justice*'.⁷⁶ Finally, as part of a new generation of statutes promulgated since 1996, the Companies Act itself references the impact of the Constitution on several occasions, with the Legislature expressly requiring that corporate law should be interpreted in a 'constitutional setting'.⁷⁷

As Du Plessis contends, constitutional interpretation surely calls for a new approach - one that has matured beyond the conventional canons of construction.⁷⁸ He refers to this approach, whereby the principles for the interpretation of statutes are to be derived from the Constitution, as a 'teleological enunciation of a procedure of statutory-cum-constitutional interpretation..., namely the reading of statutes in conformity with the

⁷³ Section 8(3)(a), Constitution of the Republic of South Africa, 1996. Conversely, the court may also develop rules of the common law to limit such a right, provided that the limitation is in line with section 36 of the Constitution. S 8(3)(b). See discussion below at text to note 165 and onwards regarding the impact of this provision in relation to the interpretation of the common law.

⁷⁴ Section 165(1), Constitution of the Republic of South Africa, 1996.

⁷⁵ Section 165(2), Constitution of the Republic of South Africa, 1996.

⁷⁶ Section 173, Constitution of the Republic of South Africa, 1996. Emphasis added.

⁷⁷ *Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa and Another v Bestvest 153 (Pty) Ltd* 2012 (5) SA 497 (WCC) (21857/2011, 2106/2012) [2012] ZAWCHC 139 par [21].

⁷⁸ Du Plessis (n2) par 327.

constitution.⁷⁹ The supreme Constitution does not deprive statutes of their worth, but ‘give[s] them new direction.’⁸⁰

Reading or interpreting a provision in conformity with the Constitution is trellised by a presumption of constitutionality, in terms of which a provision which is at first glance unconstitutional may survive scrutiny if it could be read ‘in conformity with the Constitution without distorting it or unduly straining its plain meaning’.⁸¹ This approach was authoritatively decided by Harms DP, speaking for the SCA in *Minister of Safety and Security v Sekhoto*,⁸² where it was emphasised that ‘[j]udicial officers must prefer an interpretation of legislation that falls within constitutional bounds over one that does not, provided it can be reasonably ascribed to the section.’

Thus, the courts may interpret a word or phrase in a more restrictive sense (a reading-down) or in a more extensive sense (a reading-up).⁸³ Along the same lines, if there is more than one conflicting interpretation of a statutory provision, naturally the one which best promotes the spirit, purport and objects of the bill of rights is the preferred approach.⁸⁴ It is also possible for the court to ‘read in’ certain words in order to save a provision from invalidity on constitutional grounds. This, however, must entail a ‘reasonably possible’, ‘non-distortive’, not ‘unduly strained’ reading in conformity with the Constitution.⁸⁵ Where it can be avoided the courts appear loath to read

⁷⁹ Du Plessis (n2) par 327.

⁸⁰ Du Plessis (n2) par 327.

⁸¹ Du Plessis (n2) par 330.

⁸² *Minister of Safety and Security v Sekhoto* 2011 (5) SA 367 at para 15.

⁸³ Du Plessis (n2) par 330. Du Plessis here refers to the example of *Daniels v Campbell* 2004 7 BCLR 735 (CC), 2004 5 SA 331 (CC) where the term “spouse” as it is used in the Maintenance of Surviving Spouses Act 27 of 1990 was considered. The court concluded that, to save a provision that would otherwise be considered unconstitutional and struck down, it was necessary to read this term in an extensive way, such as to include a Muslim marriage not officially solemnised in terms of the Marriage Act 25 of 1961.

⁸⁴ *Wary Holdings (Pty) Ltd v Stalwo (Pty) Ltd* 2008 11 BCLR 1123 (CC).

⁸⁵ Du Plessis (n2) par 330.

words in accordance with what Du Plessis terms a narrow understanding of ‘interpretation’ which does not allow for any words to be changed.⁸⁶

These processes of restricting or extending the scope of statutory provisions are, however, aimed at rescuing provisions from invalidity on constitutional grounds, which is not what this chapter is concerned with. The argument is not that the duties contained in the Companies Act will require any such rescue mission. But, as Du Plessis contends, ‘[t]he decisive question of statutory interpretation no longer is what the legislature intended a statute to mean, but which one of the possible meanings of the text is most compatible with the Constitution.’ Du Plessis argues that this will only be the case where the constitutionality of a statutory provision is challenged, but then again, as he puts it ‘the radiating effect of the supreme Constitution, like the perpetuity of statute law, is always present in every situation where legislation is construed, on account of section 39(2) of the Constitution. Irrespective of the interpreter’s surmise of what the legislature intended, statute law must be given effect to in a manner promoting the spirit, purport and objects of the bill of rights.’⁸⁷

⁸⁶ This may be either a sound approach which aligns with the separation of powers doctrine, or too conservative depending on which argument one favours. Moseneke J had the following warning to offer in favour of a remedially rectifying a statute as opposed to reading it in conformity with the Constitution: “Another important consideration relates to the rule of law. The problem of readily importing interpretations piecemeal into legislation is the precedent it sets. Courts below will follow the lead and readily interpret rather than declare invalid statutes inconsistent with the Constitution. However, constitutional re-interpretation does not come to this Court for confirmation. The result may be that high courts develop interpretations at varying paces and inconsistently. This makes for an even more fragmented jurisprudence and would have deleterious effects on how people regulate their affairs. It is highly undesirable to have an institution as important as marriage recognised for some people in some provinces and not in others. The rule of law requires legal certainty.” See *Daniels v Campbell* 2004 (5) SA 331 (CC) at par [104].

⁸⁷ Du Plessis (n2) par 331.

The constitution has also changed our understanding of ‘clear and unambiguous language’, with many crucial provisions of its text drafted in language that is anything but clear and unambiguous. This is deliberately so as values, one could argue, are incapable of being expressed in clear and unambiguous terms and what is more, the Constitution is ‘a durable text the expansively formulated and thus inevitably ambiguous provisions of which are meant to cater for an inestimable array of exigencies for a long time to come.’⁸⁸

Be this as it may, a regard for Constitutional values cannot be taken as *carte blanche* by a court interpreting a statutory provision. Thus, the Constitutional Court in *South African Police Service v Public Servants Association* warned that:

Interpreting statutes within the context of the Constitution *will not require the distortion of language so as to extract meaning beyond that which the words can reasonably bear*. It does, however, require that the language used be interpreted as far as possible, and without undue strain, so as to favour compliance with the Constitution. This in turn will often necessitate close attention to the . . . and institutional context in which the provision under examination functions. In addition it will be important to pay attention to the specific factual context that triggers the problem requiring solution.⁸⁹

The impact of this type of analysis on juristic persons and company directors has focussed mainly on human rights abuses and the potential liability for such abuses. In fact, this question has generated extensive debate in the South African context given the progressive nature of the

⁸⁸ Du Plessis (n2) par 331.

⁸⁹ 2007 (3) SA 521 (CC) ([2007] 5 BLLR 383; [2006] ZACC 18) at par [20] (emphasis added). See also *Serious Economic Offences & Others v Hyundai Motor Distributors (Pty) Ltd & Others: In re Hyundai Motor Distributors (Pty) Ltd & Others v Smit NO & Others* 2001 (1) SA 545 (CC), 2000 (10) BCLR 1079 (CC) at [21] – [24]; *University of Stellenbosch Law Clinic v Minister of Justice* 2016 (6) SA 596 (CC) at [137].

Constitution and the Bill of Rights.⁹⁰ A link between the Constitutional imperative and corporate governance values espoused by King IV is more tangential but that is not to say that at least certain components of a good governance regime haven't become constitutional imperatives. What comes to mind are in fact issues that were directly mentioned by King III and again reiterated in King IV as being required of any company operating in a Constitutional dispensation underpinned by the values of the South African Constitution - such as corporate social responsibility, appropriate risk management, stakeholder management and the environmental impact of the company.

⁹⁰ See for example M Gwanyanya 'The South African Companies Act and the realisation of corporate human rights and responsibilities' (2015) 18(1) *PELJ* 3101. As the authors of Blackman contends, 'one can certainly debate how far this should go in relation to the interpretation of directors' duties. The low-water mark would be that a director has a duty to ensure that the company adheres to the Constitution as part of its obligations to conduct its business in a lawful manner.' See also: D Bilchitz 'Corporate law and the Constitution: Towards binding human rights responsibilities for corporations' (2008) 125(4) *SALJ* 754; D Bilchitz *Human Rights Obligations of Business: Beyond the Corporate Responsibility to Respect?* (2013); IM Esser 'Corporate social responsibility: A company law perspective' (2011) 23(3) *SA Merc LJ* 317; J Katzew 'Crossing the divide between the business of the corporation and the imperatives of human rights—the impact of section 7 of the Companies Act 71 of 2008' (2011) 128(4) *SALJ* 686; L Muswaka 'The corporate responsibility for human rights: A conceptual framework' (2014) 5(3) *MJSS* 219; SR Ratner 'Corporations and human rights: A theory for legal responsibility' (2001) 111 *Yale LJ* 443; CJ Roederer CJ 'Post-matrix legal reasoning: Horizontality and the rule of values in the South African law' (2003) 19(1) *SAJHR* 57; JG Ruggie 'Business and human rights: The evolving international agenda' (2007) 101 *AJIL* 819; L Smit 'Human rights litigation against companies in South African courts: A response to *Mankayi v AngloGold Ashanti* 2011 (3) SA 237 (CC)' (2011) 27(2) *SAJHR* 354; B Stephens 'Corporate liability: Enforcing human rights through domestic litigation' (2000–2001) *Hastings Int'l & Comp L Rev* 401; MD Chirwa 'The long march to binding obligations of transnational corporations in international human rights law' (2006) 22(1) *SAJHR* 76.

c. The Role of Extrinsic or Extra-Textual Material in Interpreting Legislation

The South African Law Reform Commission, in its review of the Interpretation Act 33 of 1957 dealt extensively with the role of extrinsic material when interpreting statutes.⁹¹ The Committee refers to Bennion's⁹² description of what might constitute 'enacting history', namely materials 'assumed to be within the contemplation of Parliament when it passed the Act'.⁹³ Such enacting history would, according to Bennion, comprise reports and other material on which legislation is based, reports of parliamentary debates, explanatory memoranda and 'other contemporaneous material upon which Parliament may be presumed to have acted.'⁹⁴

These materials are described as the scaffolding used in the construction of the statute, and in an ideal world such scaffolding would no longer serve any purpose once the 'building' is erected – the central idea of legislation being 'to provide the citizen or adviser with a structure which *in itself* constitutes a basis upon which the person bound can safely stand.'⁹⁵ However this idea has proven itself to be idealistic, and is defeated by the shortcomings of language and the competence of the legislators, not to mention the fact that these drafters seek to regulate a future that remains at least to some extent beyond their contemplation.⁹⁶

The extent to which sources outside of the statute should be referenced in its interpretation has not been without controversy. Historical interpretation in the South African context tends to be focussed on the origin or genesis of

⁹¹ The South African Law Reform Commission Discussion Paper 112, 'Statutory Revision: Review of the Interpretation Act 33 of 1957 (Project 25)', September 2006 (ISBN:0-621-36904-7) at page 98 - 144 available online at http://www.justice.gov.za/salrc/dpapers/dp112_interpretation.pdf.

⁹² The Commission at p 98 references Bennion (n8) 520.

⁹³ South African Law Reform Commission Discussion Paper 112 at p98.

⁹⁴ South African Law Reform Commission Discussion Paper 112 at p98.

⁹⁵ Bennion (n8) 520.

⁹⁶ Bennion (n8) 520.

the text and the deliberations preceding it, 'custom, references to the predecessors and successors of a provision to be construed and surrounding circumstances more or less coinciding with the adoption of the provision have all been held to be allowable historical *indicia* of the meanings that may be attributed to a provision.'⁹⁷ On the other hand, apart from in the context of constitutional analysis, the courts have been less accepting of so called *travaux préparatoires* and for reasons discussed below genetic interpretation⁹⁸ should best be 'employed with circumspection'.⁹⁹

For purposes of this discussion a number of these sources or references are particularly significant. The role of custom as an aid to interpretation will be considered as it may be in this sense that the contents of the King Report may become a legitimate guide to interpretation. The extent to which the surrounding circumstances that existed at the time that the statute was passed may be consulted will likewise be considered, as will the genesis of the text and so called *travaux préparatoires*. The latter will be considered because the debates and arguments related to the inclusion of these materials shed light on the justification of their use and may usefully be transposed to illuminate the discussion on hand.

i. Custom

In instances where a statute could reasonably be interpreted in more than one way, South African courts have been willing to invoke custom to 'tip the balance'.¹⁰⁰ In other words, only where a provision is obscure or unclear, has

⁹⁷ Du Plessis (n2) par 369.

⁹⁸ Or an interpretation focussed on the genesis or origins of the text. See Du Plessis (n2) par 369.

⁹⁹ Du Plessis (n2) par 374.

¹⁰⁰ Mason AJA in the judgement of *R v Lloyd* 1920 AD 474 at 486. And see Du Plessis (n2) par 369.

the invocation of custom ever been considered appropriate.¹⁰¹ In order to invoke a custom, it need not have evolved prior to the commencement of a statutory provision.¹⁰² Du Plessis explains that customs may evolve on either a horizontal or a vertical level. In instances where customs evolve ‘because subjects live up to them’, they are considered horizontal whereas vertical customs are those that come into being ‘as a result of the conduct of authorised functionaries of the state’.¹⁰³ He correctly points out that the cases that deal with the interpretative value of custom seem to refer only to those customs that evolved on a vertical level.¹⁰⁴ This would tend to exclude the possibility of the King Code to be consulted by virtue of its being ‘commercial custom’.

ii. Similar Provisions in Other Statutes

It is not uncommon for the courts to refer to similar or identical provisions found in predecessors to the statute in question, provided that the two pieces of legislation are closely associated or *in pari materia*.¹⁰⁵ When

¹⁰¹ See Du Plessis (n2) par 370 where the author cites the following authorities: *R v Detody* 1926 AD 198 202–203; *Dinkel v Union Government* 1929 AD 150 165; *Minister of Justice v Breytenbach* 1942 AD 175 190; *Ernst v Commissioner for Inland Revenue* 1954 1 All SA 340 (A); 1954 1 SA 318 (A) 324A–B; *Ellert v Commissioner for Inland Revenue* 1957 1 All SA 468 (A); 1957 1 SA 483 (A) 490; *Consolidated Diamond Mines of SWA v Administrator SWA* 1958 4 SA 572 (A) 658H–659C; *Secretary for Customs & Excise v Millman* 1975 3 All SA 536 (A); 1975 3 SA 544 (A) 551F–G; *Stellenbosch Wine Trust Ltd v Oude Meester Group Ltd* 1977 2 All SA 366 (C); 1977 2 SA 221 (C) 245H; *Tseleng v Chairman, Unemployment Insurance Board* 1995 2 BCLR 138 (T) 149J–150B; 1995 3 SA 162 (T)

¹⁰² *Vorster v Muller & the Minister of Mines* supra 129–130; *Randfontein Estates Gold Mining Co Witwatersrand Ltd v Minister of Finance* supra 84; *R v Pretoria Timber Co (Pty) Ltd* 1950 1 All SA 1 (A); 1950 3 SA 163 (A) 165 175B–176H; *Webb & Ross v Gey van Pittius* supra 481D–F.

¹⁰³ Du Plessis (n2) par 370.

¹⁰⁴ Du Plessis (n2) par 370.

¹⁰⁵ *Nkabinde v Nkabinde & Nkabinde* 1944 WLD 112 122; *Johannesburg City Council v Makaya* 1945 AD 252 259; *Hleka v Johannesburg City Council* 1949 2 All SA 71 (A); 1949 1 SA 842 (A) 850; *R v von Zell (2)* 1953 4 SA 552 (A) 558F–G; *Estate Brownstein v Commissioner for Inland Revenue* 1957 3 All SA 267 (A); 1957 3 SA 512 (A) 523B–G.

incorporating provisions from one statute into another *mutatis mutandis* the courts have tended to adapt the language of the provisions being adopted only to the extent required by necessity. They have, in other words, made such changes as were necessary for the provision in question to function and have not changed it to the extent that it is 'fitting' in relation to the new provision.¹⁰⁶ The interpretation of the phrase *mutatis mutandis* has thus been held to mean 'with the necessary changes in points of detail.'¹⁰⁷ This more conservative approach is justified on the basis that fitness in a less strict sense of the word would open a wide field for speculation and there may well be room for significant variances in opinion when it comes to determining whether changes were or were not fitting. This in turn could seriously undermine legal certainty.¹⁰⁸

iii. Surrounding Circumstances

Hitherto, relevant surrounding circumstances at the time when the statute was passed may be taken into consideration when interpreting the text, provided that these circumstances are such that the court can take judicial

¹⁰⁶ Du Plessis (n2) par 370, where the author cites *Touriel v Minister of Internal Affairs Southern Rhodesia* 1946 AD 535 544; *R v Adams* 1959 3 All SA 563 (A); 1959 3 SA 753 (A) 759H; *Publications Control Board v William Heinemann Ltd* 1965 4 All SA 239 (A); 1965 4 SA 137 (A) 145F–G; *S v King* 1966 2 All SA 19 (A); 1966 1 SA 500 (A) 506B–C; *SA Master Dental Technicians Association v Dental Association of SA* 1970 3 All SA 543 (A); 1970 3 SA 733 (A) 745E–G. In *Waymark v Meeg Bank Ltd* 2003 1 All SA 518 (Tk); 2003 4 SA 114 (Tk) 530 the court spoke of "necessary alterations to fit the changed circumstances" that had to be made.

¹⁰⁷ *Touriel v Minister of Internal Affairs, Southern Rhodesia* 1946 AD 535 at 545, Feetham AJA

¹⁰⁸ *Touriel v Minister of Internal Affairs, Southern Rhodesia* 1946 AD 535 at 545, Feetham AJA

notice of them¹⁰⁹ and that they existed at the time the statute was passed.¹¹⁰ Traditionally it was only possible to take cognisance of such circumstances where the provision in question was unclear or ambiguous, but as mentioned above, surrounding circumstances may now be considered regardless the clarity of the language of a provision.¹¹¹

iv. Preceding Discussions or *Travaux Préparatoires*

In the South African context, so-called ‘preceding discussions’ included debates about a Bill in parliament, debates and reports of committees forming part of the legislative process, and reports of commissions of inquiry

¹⁰⁹ Du Plessis (n2) par 373. And see: *R v Detody* 1926 AD 198 at 208 where Innes CJ refers to “circumstances which are matter of common historical knowledge”; *SAR&H v Smith’s Coasters (Prop) Ltd* 1931 AD 113 127; *Harris v Minister of the Interior* 1952 2 All SA 400 (A); 1952 2 SA 428 (A) 457A–B. For a more indirect application of this canon, see also *Malan v Die Oranje-Vrystaatse Ongedierte Bestrydings & Wildbewaringsvereniging* 1976 1 SA 830 (O) 836A–F; *Komani v Bantu Affairs Administration Board, Peninsula Area* 1980 2 All SA 500 (A); 1980 4 SA 448 (A) 463F–H; *Bamford v Minister of Community Development & State Auxiliary Services* 1981 3 SA 1054 (C) 1057F–H; *Minister of Land Affairs v Slamdien* 1999 4 BCLR 413 (LCC) pars 14 17–26. See also re ‘judicial notice’: *Consolidated Diamond Mines of SWA Ltd v Administrator, SWA* 1958 4 SA 572 (A) 657F–H; *Diepsloot Residents’ & Landowners’ Association v Administrator, Tvl* 1994 2 All SA 299 (A); 1994 3 SA 336 (A) 347D–E; *Christian Lawyers Association of SA v Minister of Health* 1998 11 BCLR 1434 (T) 1438H–1440H.

¹¹⁰ Du Plessis points out that, although subsequent developments could not be taken into account as ‘surrounding circumstances’ they may well be admissible as custom. See: Du Plessis (n2) par 373 where the author references the judgement of *Cape Provincial Administration v Honiball* 1942 AD 1 16; *Peri-Urban Areas Health Board v Breet* 1958 2 All SA 224 (T); 1958 3 SA 783 (T) 788A–B.

¹¹¹ Du Plessis (n2) par 373, and see: *University of Cape Town v Cape Bar Council* 1986 2 All SA 619 (A); 1986 4 SA 903 (A) 914D.

that gave rise to the legislation.¹¹² As a rule, the courts did not allow the use of such legislative debates when interpreting legislation.¹¹³

In considering the interpretation of the Constitution of the Republic of South Africa 1996, Chaskalson J on behalf of the majority of the Constitutional Court justices in *S v Makwanyane*¹¹⁴ considered the argument that the debate surrounding the death penalty before commencement of constitutional negotiations formed part of the context within which the constitution should properly be interpreted. Chaskalson J referred again to the influential judgement of Schreiner J in *Jaga v Dönges, N.O. and Another*¹¹⁵ in confirming that it is permissible in interpreting statutes to have regard to the purpose and background of the legislation in question.¹¹⁶ Specifically, Schreiner JA emphasised that ‘context’ was ‘not limited to the language of the rest of the statute regarded as throwing light of a dictionary kind on the part to be interpreted. Often of more importance is the matter of the statute, its apparent scope and purpose, and, within limits, its background.’¹¹⁷

Chaskalson J also pointed out that, although debates in parliament, and statements made by ministers responsible for legislation as well as

¹¹² The South African Law Reform Commission Discussion Paper 112, ‘Statutory Revision: Review of the Interpretation Act 33 of 1957 (Project 25)’, September 2006 (ISBN:0-621-36904-7) at page 102 available online at http://www.justice.gov.za/salrc/dpapers/dp112_interpretation.pdf where the authors cite the following cases in example: *Bok v Allen* 1884 SAR 137; *Mathiba v Moschke* 1920 AD 354; *R v Ristow* 1926 EDL 168.

¹¹³ See for example *Ngcobo v Van Rensburg* 1999 (2) SA 525 (LCC) para 27 where Dodson J concludes as follows: “The weight of authority is very much against allowing such documents to be called in aid in the interpretation of a statute. This authority has received considerable academic criticism. There are also a few authorities which seem to suggest a softening of attitudes by South African Courts to certain of the documents which precede the passing of an Act.

¹¹⁴ *S v Makwanyane and Another* (CCT3/94) [1995] ZACC 3 at par [12].

¹¹⁵ *Jaga v Dönges NO and Another; Bhana v Dönges NO and Another* 1950 (4) SA 653 (A) at 662.

¹¹⁶ *S v Makwanyane and Another* (CCT3/94) [1995] ZACC 3 at par [13].

¹¹⁷ *Jaga v Dönges NO and Another; Bhana v Dönges NO and Another* 1950 (4) SA 653 (A) at 662.

explanatory memoranda providing reasons for new bills have not been admitted as background material, the courts have taken notice of reports of judicial commissions of inquiry but only for the purpose of determining the mischief that the statutory enactment under consideration was aimed at curing.¹¹⁸ He then referred to the decision of the House of Lords in *Pepper (Inspector of Taxes) v Hart and Related Appeals*,¹¹⁹ taking note of the relaxation of the exclusionary rule in the United Kingdom and other jurisdictions such as New Zealand and Australia.

Makwanyane's case however, had to do with the interpretation of the Constitution which, as the court points out, is no ordinary statute. It is the supreme law of the land and the above remarks in favour of making greater allowance for surrounding debate may therefore not be authority for the further relaxation of the exclusionary rule in South African law.¹²⁰

In the famous 1993 decision of *Pepper (Inspector of Taxes) v Hart and Related Appeals*¹²¹ referenced by the court in *Makwanyane's* case, the House of Lords considered the so-called 'exclusionary rule', in terms of which any reference to the record of Parliamentary debates for the purpose of assisting the interpretation of a statute is excluded.¹²² The arguments of counsel referred to in the judgement and the various judgements by the

¹¹⁸ *S v Makwanyane and Another* (CCT3/94) [1995] ZACC 3 at par [14] where the Chaskalson P cites the following judgements in example: *Attorney-General, Eastern Cape v Blom and Others* 1988 (4) SA 645 (A) at 668H-669F; *Westinghouse Brake & Equipment (Pty) Ltd v Bilger Engineering (Pty) Ltd* 1986(2) SA 555(A) at 562C-563A

¹¹⁹ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL).

¹²⁰ *S v Makwanyane and Another* (CCT3/94) [1995] ZACC 3 at par [14] & [15].

¹²¹ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL). The case generated much discussion, see for example: Johan Steyn 'Pepper v Hart; a Re-Examination' (2001) 21(1) *Oxford J.Leg.St.* 59; Stephan Vogenauer 'A Retreat from Pepper v Hart? A Reply to Lord Steyn' (2005) 25(4)

Oxford J.Leg.St. 629; Phillip Sales 'Pepper v Hart: A Footnote to Professor Vogenauer's Reply to Lord Steyn' (2006) 26(3) *Oxford J.Leg.St.* 585; Michael P. Healy 'Legislative Intent and Statutory Interpretation in England and the United States: An Assessment of the Impact of Pepper V. Hart' (1999) 35 *Stan.J.Int'l L.* 231; Richard Clayton 'Life after Pepper v. Hart' (1996) 1 *JR* 77.

¹²² *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL) at page 630.

Lords offer a comprehensive history of the development of the rule and its application.¹²³ First mentioned in the case of *Millar v. Taylor*,¹²⁴ the exclusionary rule is a judge-made rule of practice and until its emergence in the middle of the 18th century, the courts had willingly referenced all available means for the interpretation of statutes as *Heydon's Case*¹²⁵ illustrates.¹²⁶ The rule was later extended further to also prohibit courts from having recourse to reports made by commissioners on which legislation was based.¹²⁷ Although it was eventually relaxed, reports of commissioners and white papers could be considered 'for the purpose solely of ascertaining the mischief which the statute is intended to cure but not for the purpose of discovering the meaning of the words used by parliament to effect such cure.'¹²⁸

Lord Reid, a proponent of the exclusionary rule, defended it on practical grounds – namely that a search for illusory clarity from parliamentary debates in any potential matter that turns on the interpretation of a statute would add time and expense to the litigious process.¹²⁹ Lord Reid also questioned the true value of such debates to the interpretative process, contending that it is in fact a misnomer to say that the courts are looking for the intention of Parliament. He explained that the difficulties were more than mere practicalities. Issues that arise during parliamentary debate are

¹²³ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL) at page 630.

¹²⁴ (1769) 4 Burr. 2303, 2332.

¹²⁵ (1584) 3 Co Rep 7a.

¹²⁶ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL) at page 630.

¹²⁷ *Salkeld v. Johnson* (1848) 2 Exch. 256, 273 and see *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL) at page 630.

¹²⁸ Lord Browne-Wilkinson, *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL) at page 630 where the following cases are cited in reference: *Eastman Photographic Materials Co. Ltd. v. Comptroller-General of Patents, Designs and Trademarks* [1898] A.C. 571; *Assam Railways and Trading Co. Ltd. v. Commissioners of Inland Revenue* [1935] A.C.445, 457-458.

¹²⁹ *Beswick v. Beswick* [1968] A.C. 58, 74

rarely the same as the issues that the courts later decide and relying on the views of the promoters of a Bill as indication of parliamentary intent is dubious.¹³⁰

In spite of this, Lord Browne-Wilkinson and a majority of the Lords concluded that the reasons to make what the former termed a 'limited modification to the existing rule' outweigh any concerns.¹³¹ The court decided that 'reference to Parliamentary material should be permitted as an aid to the construction of legislation which is ambiguous or obscure or the literal meaning of which leads to an absurdity. Even in such cases references in court to Parliamentary material should only be permitted where such material clearly discloses the mischief aimed at or the legislative intention lying behind the ambiguous or obscure words'.¹³²

Significantly, the House of Lords concluded that it is specifically in light of the purposive approach to construction now adopted by the courts, and aimed at giving effect to the true intentions of the legislature that 'the fine distinctions between looking for the mischief and looking for the intention in using words to provide the remedy are technical and inappropriate. Clear and unambiguous statements made by Ministers in Parliament are as much the background to the enactment of legislation as white papers and

¹³⁰ *Black-Clawson International Ltd. v. Papierwerke Waldhof-Aschaffenburg A.G.* [1975] A.C. 591 at pp. 613-615

¹³¹ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL); [1993] A.C. 593 Page 633. These reasons were considered and summarised by Lord Browne-Wilkinson as firstly, the fact that the rule left Parliament to legislate and the courts to construe the meaning of the words enacted; second, the practical concerns related to the expense of researching Parliamentary material, third, the 'need for the citizen to have access to a known defined text which regulates his legal rights'; and finally the improbability that a source such as Hansard will at the end of the day offer helpful guidance.

¹³² *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL); [1993] A.C. 593 Page 634.

Parliamentary reports.¹³³ The Lords also dismiss any contentions that the use of Parliamentary material in construing legislation would confuse the respective roles of Parliament as law-maker and the courts as the interpreter of these laws.¹³⁴

The decision generated much discourse.¹³⁵ Lord Steyn criticised it for failing to consider important constitutional questions and he also considered the argument that the decision was the true embodiment of a purposive approach to statutory interpretation:¹³⁶

There are, however, those who believe that the relaxation of the exclusionary rule was the ultimate vindication of purposive construction. And purposive construction is like mother's milk and apple pie: who can argue against it? The reasoning in *Pepper v Hart* sought to build on the fact that official reports and white papers are admissible for the purpose of identifying the mischief to be corrected. Such reports are always admissible for what logical value they have. But the constitutional objections do not apply to such reports. They are part of the contextual scene against which parliament legislates. In any event, to present the *Pepper v Hart* issue as depending on whether one adopts a literal or purposive approach to construction is wide off the mark. By the time *Pepper v Hart* was decided, nobody supported literal methods of construction. The suggested antithesis misses the point of the fundamental and constitutional nature of the objections. The

¹³³ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL); [1993] A.C. 593 Page 634.

¹³⁴ *Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL); [1993] A.C. 593 Page 640.

¹³⁵ A comprehensive discussion of the debates and criticisms following the decision falls outside of the scope of this thesis and commentary will only be discussed to the extent that it remains relevant. See for example sources cited at note 121 above.

¹³⁶ "The Intractable Problem of The Interpretation of Legal Texts" John Lehane Memorial Lecture 2002 on 25 September 2002 at the University of Sydney available at <http://www.austlii.edu.au/au/journals/SydLRev/2003/1.html> (accessed on 7 September 2006) see also Steyn (n121) 59.

objections are not simply that a minister's view of a clause is irrelevant but that it is in principle wrong to treat it as a trump card or even relevant in the interpretative process.

Following the far-reaching developments in the recent South African context, the exact role of genetic material in interpreting statutes remains unclear. As was argued above, it may well be that the decision in *Endumeni* has the implication that such materials have now become admissible. The argument could be made that this development would be in step with the changes introduced to English law by the judgement in *Pepper v Hart*. However, as the debates surrounding this latter judgement illustrate, genetic interpretation should likely be employed with caution.¹³⁷ This seems to be the approach that the Supreme Court of Appeals in South Africa is likely to follow in future, given the more restrictive interpretation of *Endumeni*'s principles most recently endorsed by the court in *Blair Athol Homeowners Association*.¹³⁸

Also, even though it may be more acceptable to consult reports of parliamentary commissions of investigation recommending a particular legislative course,¹³⁹ this is subject to a number of conditions.¹⁴⁰ First, the

¹³⁷ Du Plessis (n2) par 374, where the author remarks: 'In the absence of "objective" evidence regarding this history genetic interpretation can be of limited value only. Each of those who participated in authoring the text is likely to have an unusably subjective perception of what the text is capable of saying. Debate and conflict of opinion often characterise the deliberations preceding the adoption and passing of a (statutory or constitutional) text. Opinions among the members of the body authoring the text will thus inevitably diverge (even in respect of formulations to which they agreed unanimously).'

¹³⁸ *The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* 2019 (3) SA 398 (SCA).

¹³⁹ Du Plessis (n2) par 374. And see: *Westinghouse Brake & Equipment (Pty) Ltd v Bilger Engineering (Pty) Ltd* 1986 2 SA 555 (A) 562J–563A. See also *S v Mpetha* 1985 2 All SA 402 (A); 1985 3 SA 702 (A) 712H–713D; *Trident Steel (Pty) Ltd v John* 1987 8 ILJ 27 (W) 34G–I.

¹⁴⁰ *Attorney-General, Eastern Cape v Blom* (83/88) [1988] ZASCA 83; [1988] 2 All SA 592 (A) (30 August 1988).

language of the provision may not be clear and unambiguous, and there must be a clear link between the findings and recommendation of the commission and the legislation that was passed at the end of the day. The court would then be able to consider such findings for purposes only of ascertaining the mischief that the provision in question aims to address.¹⁴¹

The analysis above shows that the courts have traditionally treated extrinsic material with a fair degree of circumspection. Whereas the practices that have developed under the auspices of the King Codes and Reports over the past few decades may be considered 'custom' and the Codes themselves could be considered 'surrounding circumstances' such that a court could take judicial notice of, many of the warnings and concerns pertaining in particular to *travaux preparatoires* may well transfer to any debate surrounding the importations of more detailed sections of the Code. It may well be that the impact of *Endumeni* is such that much of the reach of that judgement as it pertains to these issues has not been decided by the courts. Having considered the legal backdrop against which the Companies Act will be interpreted, the chapter will now turn to the relevant provisions of the Act itself and consider their impact.

3 Relevant Statutory Provisions

The duties that directors have to act with care, skill and diligence and in the best interests of the company were discussed in greater depth in chapters 3 and 4 preceding this analysis. However, because the exact wording of the Act is again of concern, extracts from the Act will be included again for ease of reference.

¹⁴¹ *Attorney-General, Eastern Cape v Blom* (83/88) [1988] ZASCA 83; [1988] 2 All SA 592 (A) (30 August 1988); 1988 (4) SA 645 (A) at 668 - 669.

Section 76(3)(c) requires a director of a company when acting in that capacity, to exercise the powers and perform the functions of director ‘in the best interests of the company’¹⁴² and ‘with the degree of care, skill and diligence that may reasonably be expected of a person carrying out the same functions in relation to the company as those carried out by that director; and having the general knowledge, skill and experience of that director’.¹⁴³

Section 76(4) may also be relevant as will be explained in chapter 7 below. As previously mentioned¹⁴⁴ that section imports a version of the ‘business judgement rule’ into the legislation and determines that a director will have satisfied his obligations in terms of Section 76(3)(b) and (c) if ‘the director has taken reasonably diligent steps to become informed about the matter’ and ‘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.’

Section 77 then determines that a director will be liable ‘in accordance with the principles of the common law relating to breach of a fiduciary duty, for any loss, damages or costs sustained by the company as a consequence of any breach by the director of a duty contemplated in section76(3) (b); or in accordance with the principles of the common law relating to delict for any loss, damages or costs sustained by the company as a consequence of any breach by the director of a duty contemplated in section 76(3)(c)...’¹⁴⁵

When considering these sections, it is clear that the Act makes no mention of the King Code or Report in either section 76 or section 77. Any court referring to its provisions would therefore be ‘reading in’ words that are not

¹⁴² Section 76(3)(b).

¹⁴³ Section 76(3)(c)(i) – (ii).

¹⁴⁴ See chapter 7 at text to note 80 and onwards.

¹⁴⁵ Section 77(2)(a) – (b).

expressly found in the act. In particular, the duty of care, skill and diligence would have to be interpreted to include a phrase such as ‘with due reference to the norms and principles set out in the King Code and Report’. The duty to act in the best interests of the company would for example then include words such as ‘with those interests encompassing multiple stakeholders as envisaged in the King Code and Report’ or perhaps something more generic such as ‘reference to the norms and principles of accepted best practices in corporate governance’.

Justification for this is perhaps to be found in the purposes of the Act, that quite clearly indicate that the legislation is aimed at ‘encouraging *transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation*’.¹⁴⁶ Further justification may be found in the form of the constitutional imperative. In its policy paper, the South African Department of Trade and Industry¹⁴⁷ state plainly that the framework of company law should reflect the ‘recognition that a company is a social as well as an economic institution, and accordingly that a company’s pursuit of economic objectives should be constrained by social and environmental imperatives’¹⁴⁸ and this was reiterated in the purposes to an extent as the legislation seeks to ‘reaffirm the concept of the *company as a means of achieving economic and social benefits*’.¹⁴⁹

¹⁴⁶ Section 7.

¹⁴⁷ *South African Company Law for the 21st Century – Guidelines for Corporate Law Reform* Government Gazette 26493 of 23 June 2004 available online at https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf.

¹⁴⁸ *South African Company Law for the 21st Century – Guidelines for Corporate Law Reform* at 27.

¹⁴⁹ Section 7.

The Companies Act sets out the scope of its application in section 5 which determines that the Act must be interpreted and applied in a manner that gives effect to the following purposes set out in section 7:¹⁵⁰

- (a) *promote compliance with the Bill of Rights* as provided for in the Constitution, in the application of company law;
- (b) promote the development of the South African economy by—
 - (i) encouraging entrepreneurship and *enterprise efficiency*;
 - (ii) creating flexibility and simplicity in the formation and maintenance of companies; and
 - (iii) encouraging *transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation*;
- (c) promote innovation and investment in the South African markets;
- (d) reaffirm the concept of the *company as a means of achieving economic and social benefits*;
- (e) continue to provide for the creation and use of companies, in a manner that enhances the economic welfare of South Africa as a partner within the global economy.
- (f) promote the development of companies within all sectors of the economy, and encourage active participation in economic organisation, management and productivity;
- (g) create optimum conditions for the aggregation of capital for productive purposes, and for the investment of that capital in enterprises and the spreading of economic risk;
- (h) provide for the formation, operation and accountability of non-profit companies in a manner designed to promote, support and enhance the capacity of such companies to perform their functions;
- (i) *balance the rights and obligations of shareholders and directors* within companies;
- (j) encourage the *efficient and responsible management* of companies;

¹⁵⁰ S 5(1), Companies Act 71 of 2008.

- (k) provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders; and
- (l) provide a predictable and effective environment for the efficient regulation of companies.¹⁵¹

As discussed above, South African courts have emphasized the fact that the Act is to be interpreted ‘through the prism of the Constitution.’¹⁵² Section 7 clearly requires this¹⁵³ and the purposes listed in that section should also be read against the backdrop of preparatory documents which preceded the legislation. A policy paper published by the South African Department of Trade and Industry entitled ‘South African Company Law for the 21st Century – Guidelines for Corporate Law Reform’¹⁵⁴ (hereafter ‘the policy paper’) stated that the new act strived to achieve ‘a clear, facilitating, predictable and consistently enforced law’.¹⁵⁵ The Policy Paper further sets out numerous principles which informed the Explanatory Memorandum to the Companies Bill, 2007 and subsequently the Act itself. It is noteworthy that the policy paper also stated that the framework of company law should reflect the ‘recognition that a company is a social as well as an economic institution, and accordingly that a company’s pursuit of economic objectives should be constrained by social and environmental imperatives’.¹⁵⁶

¹⁵¹ S 7(a) – (l), Companies Act 71 of 2008, emphasis added.

¹⁵² *Booyesen v Jonkheer Boerewynmavery (Pty) Ltd and Another* [2017] 1 All SA 862 (WCC) para 41.

¹⁵³ See s7(a). See also: *Minister of Environmental Affairs v Recycling and Economic Development Initiative of South Africa NPC*, *Minister of Environmental Affairs v Kusaga Taka Consulting (Pty) Ltd* 2018 (3) SA 604 (WCC).

¹⁵⁴ Government Gazette 26493 of 23 June 2004 available online at https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf.

¹⁵⁵ South African Company Law for the 21st Century – Guidelines for Corporate Law Reform at 11. And see: *Henochnberg on the Companies Act 71 of 2008* (Issue 18 2018) 50.

¹⁵⁶ South African Company Law for the 21st Century – Guidelines for Corporate Law Reform at 27.

It goes without saying that the objects of an act will not always align neatly and that some may even clearly conflict. So, to name one example, it is entirely possible that an act which may ‘encourage[e] entrepreneurship and enterprise efficiency’ could undermine ‘transparency and high standards of corporate governance’. The wording of the objects in section 7 thus present two potential challenges, the first being that conflicting objects may require the court to rank or strike a balance between competing goals (and judges will often not possess of adequate information to make these far reaching policy decisions – nor it could be argued, should they be required to do so). Secondly, the stated purposes are relatively generic and devoid of detail or explanation. They will often shed no real light on how a provision should ideally be interpreted.

In answer to these concerns, the authors of Blackman suggest that section 7 ‘has been provided in order to assist judicial interpreters to understand what the general purpose of the legislature was when adopting the act’ and that the purposes will ‘contextualise and colour the interpretation of particular provisions rather than override them’.¹⁵⁷ The manner in which the courts have engaged with the purposes since the promulgation of the Act would appear to bear this out.¹⁵⁸

Section 158 which bears the heading ‘Remedies to promote the purpose of the Act’ emphasises a purposive approach¹⁵⁹ to the interpretation of the Act.

¹⁵⁷ JL Yeats (ed) *Commentary on the Companies Act of 2008* (Juta 2018) 1-52.

¹⁵⁸ Several judgements illustrate how the courts have engaged with the purposes of the Companies Act set out in Section 7: See for example: *Sibakhulu Construction (Pty) Ltd v Wedgewood Village Golf Country Estate (Pty) Ltd* 2013 (1) SA 191 (WCC) para 23 – 27 where the court considered the purposes of the Act and then looked practically at the implications if multiple courts could have jurisdiction over matters affecting the status of a company. And see *Newlands Surgical Clinic (Pty) Ltd v Peninsula Eye Clinic (Pty) Ltd* 2015 (4) SA p45 86/2014 [2015] ZASCA 25 where the court took account of contextual material such as the legislative history but reiterated that the court should not stray into the territory of inventing or reading in too liberally at par [26] – [27].

¹⁵⁹ See below at note 165 and onwards.

In terms of that section, ‘a court must develop the common law as necessary to improve the realisation and enjoyment of rights established by [the] Act’,¹⁶⁰ and a court¹⁶¹ ‘must promote the spirit, purpose and objects of [the]Act’.¹⁶² In instances where it is possible that any provision of the Act (or other document in terms of the Act) can be ‘reasonably construed’ to have more than one meaning, the preferred meaning must be that which ‘best promotes the spirit and purpose of [the] Act, and will best improve the realisation and enjoyment of rights.’¹⁶³

Finally, it bears mention that the express purposive provisions of the Act appear not to be conclusive. In this regard, the South African Law Reform Commission concluded that:

Express purpose provisions provide a more detailed description of the legislative purpose than, for example, the long title or preamble, but it can never be decisive in isolation. To take such a view would merely be to create a new and sophisticated version of literal interpretation. The interpreter not only has to read the legislative text as a whole, but must also consult all available and relevant internal and external information or aids (dealt with in detail below) during interpretation. Although the

¹⁶⁰ S 158(a).

¹⁶¹ The subsection also applies to “the Commission, the Panel, [and] the Companies Tribunal” all bodies established by the Act for purposes of regulation, administration and dispute resolution.

¹⁶² S 158(b)(i).

¹⁶³ S 158(b)(ii). See for an example of such an interpretation *Swart v Beagles Run Investments 25 (Pty) Ltd* 2011 (5) SA 422 (GNP) [2011] ZAGPPHC 103; 26597/2011 (30 May 2011) an application to initiate business rescue proceedings where the court concluded in para [41] that “where an application for business rescue ... entails the weighing-up of the interests of the creditors and the company the interests of the creditors should carry the day.” Along similar lines, admittedly all decided in the context of business rescue proceedings, see: *Welman v Marcelle Props 193 CC and Another* [2012] JOL 28714 (GSJ); (33958/2011) [2012] ZAGPJHC 32 (24 February 2012) paras [16], [25] and [28]; *Employees of Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd* 6418/2011 8 May 2012 (GNP); 6418/2011, 18624/2011, 66226/2011, 66226/2011, 66226A/11) [2012] ZAGPPHC 359 (16 May 2012) para [12]; and *Mouritzen v Greystone Enterprises (Pty) Ltd* 2012 (5) SA 74 (KZD); [2012] ZAKZDHC 103; [2012] ZAKZDHC 34 (8 June 2012) para [18].

interpreter cannot rely on the purpose provision to ascertain the purpose of legislation, it could be used as an additional tool to find the object and purpose of the enactment. However, the inclusion of a purpose provision will also be important in a more substantive sense: It will force judges, judicial officers and all interpreters of legislation to accept a purposive and value-coherent methodology of interpretation that is fully in line with the demands of the new constitutional order (more specifically s 39(2) of the Constitution).¹⁶⁴

4 Interpreting and Developing the Common Law

It has always been the responsibility of the courts to develop and apply the common law to reflect the norms and address the needs of a changing society.¹⁶⁵ The mandate to develop the common law, which is now contained in Section 173 of the Constitution, merely reiterates this standing role of the courts,¹⁶⁶ although since the coming into force of the 1996 Constitution the function must now be exercised in a manner that promotes the spirit, purport and objects of the Bill of Rights.¹⁶⁷ The courts have, on numerous occasions, considered the impact that this constitutional imperative might have on the interpretation of the common law. In the seminal case of *Carmichele v Minister of Safety and Security*¹⁶⁸ the

¹⁶⁴ Discussion Paper 112: Review of the Interpretation Act 33 OF 1957 (SA Law Reform Commission 2006) available online at http://www.justice.gov.za/salrc/dpapers/dp112_interpretation.pdf Page 40 par 2.50.

¹⁶⁵ *Amod v Multilateral Motor Vehicle Accidents Fund* (CC) 27-8-1998 (case CCT 4/98 unreported) at [22].

¹⁶⁶ *Blower v Noorden* 1909 TS 890 at 905; *Pearl Assurance v Union Government* 1934 AD 560 at 563. And see in general also: Malcolm Wallis 'The Common Law's Cool Ideas for Dealing with Ms Hubbard' (2015) (4) *SALJ* 940, 942.

¹⁶⁷ Section 39(2) of the Constitution, 1996. See also: *Amod v Multilateral Motor Vehicle Accidents Fund* (CC) 27-8-1998 (case CCT 4/98 unreported) at [22].

¹⁶⁸ *Carmichele v Minister of Safety and Security* (CCT 48/00) [2001] ZACC 22; 2001 (4) SA 938 (CC).

Constitutional Court was asked to developed ‘wrongfulness’ in the context of the South African law of delict(tort) to allow for vicarious liability for the Minister. The court set out the general approach to the application of section 39(2), noting that there are two stages to the inquiry that the court must undertake:

The first stage is to consider whether the existing common law, having regard to the section 39(2) objectives, requires development in accordance with these objectives. This inquiry requires a reconsideration of the common law in the light of section 39(2). If this inquiry leads to a positive answer, the second stage concerns itself with how such development is to take place in order to meet the section 39(2) objectives.¹⁶⁹

There was some debate in academic circles about the exact role of the constitution and the extent to which it could or should prompt the courts to undertake a wholesale ‘constitutional revamp’ of existing common law.¹⁷⁰ Wallis J addressed the issues in an article commenting on the cases of *Hubbard v Cool Ideas 1186 CC*¹⁷¹ and *Cool Ideas 1186 CC v Hubbard*.¹⁷² He reminds us that ‘the law was not invented in South Africa in 1994’¹⁷³ and that there was a substantive common law in place which was based on equitable principles and which even today, would adequately serve to

¹⁶⁹ *Carmichele v Minister of Safety and Security* (CCT 48/00) [2001] ZACC 22; 2001 (4) SA 938 (CC) at [40].

¹⁷⁰ The debate was in particular between Prof Anton Fagan and Judge Dennis Davis in a series of articles on the subject. The finer nuances of the debate are technical and will not serve to further illuminate the questions posed by this research. See: Anton Fagan ‘The secondary role of the spirit, purport and objects of the Bill of Rights’ (2010) 127 *SALJ* 611; Dennis Davis ‘How many positivist legal philosophers can be made to dance on the head of a pin? A reply to Professor Fagan’ (2012) 129 *SALJ* 59; Anton Fagan ‘A straw man, three red herrings and a closet rule-worshipper —A rejoinder to Davis JP’ (2012) 129 *SALJ* 788 and Dennis Davis ‘The importance of reading—A rebutter to the jurisprudence of Anton Fagan’ (2013) 130 *SALJ* 52.

¹⁷¹ *Hubbard v Cool Ideas 1186 CC* 2013 (5) SA 112 (SCA).

¹⁷² *Cool Ideas 1186 CC v Hubbard* 2014 (4) SA 474 (CC).

¹⁷³ Wallis (n166) 941.

protect many of the rights contained in the Bill of Rights. In the case in question, he argues that reliance on the Constitution was not appropriate as the parties to the case had adequate remedies in common law which they had failed to pursue.¹⁷⁴ He concludes that ‘we will only achieve a mature jurisprudential understanding of the relationship between the constitution, the spirit, purport and objects of the Bill of Rights and the common law through a structured analytical approach that affords each its proper role in our jurisprudence.’¹⁷⁵

The responsibility of the courts to develop the common law should generally be exercised with restraint:

Judges can and should adapt the common law to reflect the changing social, moral and economic fabric of the country. Judges should not be quick to perpetuate rules whose social foundation has long since disappeared. Nonetheless there are *significant constraints on the power of the judiciary to change the law* . . . In a constitutional democracy such as ours it is the Legislature and not the courts which has the major responsibility for law reform . . . The judiciary should confine itself to those *incremental changes* which are necessary to keep the common law in step with the dynamic and evolving fabric of our society.¹⁷⁶

The Constitutional Court has cautioned that ‘the major engine for law reform should be the Legislature not the Judiciary’¹⁷⁷ and Wallis reiterates that ‘the development of the common law is an adjunct to this process, not the driver of it.’¹⁷⁸ It does happen that the law might require adaptation to meet changing needs and that it might in certain instances not be feasible to wait for legislative intervention for any number of reasons. It is in these instances

¹⁷⁴ Wallis (n166) 941.

¹⁷⁵ Wallis (n166) 941.

¹⁷⁶ Iacobucci J in *R v Salituro*, (1992) 8 CRR (2d) 173, cited with approval by Kentridge AJ in *Du Plessis v De Klerk* 1996 (3) SA 850 (CC) at [15]. Emphasis added.

¹⁷⁷ *Carmichele v Minister of Safety and Security* (CCT 48/00) [2001] ZACC 22; 2001 (4) SA 938 (CC) at [35].

¹⁷⁸ Wallis (n166) 944.

where ‘the courts step into that gap and by a process of adaptation – usually slow but occasionally more extreme – make the necessary changes that society demands, subject always to the legislature’s ability to alter the result by legislation.’¹⁷⁹

In developing the common law, the court should not do more than what is required to resolve the matter before it, as the ‘development of the common law occurs best when it proceeds from case to case rather than in leaps and bounds, because it is rare for a court to have the degree of knowledge of the full implications of its decision that sweeping reform requires’.¹⁸⁰ In terms of the application of the constitution Wallis warns that a court should engage in a development of the common law only if it is clear that it has received all the factual material relevant to the particular problem, and that any potential developments remain rooted in a concrete dispute in a specific matter. He notes that ‘[i]t is rare that proceedings on exception or a stated case provide sufficiently comprehensive material to determine complex issues such as the impact of the Constitution on common law rules.’¹⁸¹

Though the possibility of developing the common law to encapsulate elements of the governance code may sound attractive, Lord Scarman’s general warning endures:¹⁸²

It is an attractive, ingenious suggestion — but, in my judgment, unsound. For so radical a reform can be made neither by judges nor by modification of rules of court. It raises issues of social, economic and financial policy not amenable to judicial reform, which will almost certainly prove to be controversial and can be resolved by the

¹⁷⁹ Wallis (n166) 944. The challenge is now compounded as it has become necessary, in this continuing process of development, to also identify those issues that will be affected by the need to ‘give effect to the spirit, purport and objects of the Bill of Rights’.

¹⁸⁰ Wallis (n166) 967.

¹⁸¹ Wallis (n166) 967.

¹⁸² In *Lim Poh Choo v Camden and Islington Local Health Authority* [1980] AC 174.

legislature only after full consideration of factors which cannot be brought into clear focus, or be weighed and assessed, in the course of the forensic process. The judge—however wise, creative, and imaginative he may be—is “cabin’d, cribb’d, confin’d, bound in” not, as was Macbeth, to his “saucy doubts and fears” but by the evidence and arguments of the litigants. It is this limitation, inherent in the forensic process, which sets bounds to the scope of judicial law reform.

5 Conclusion

This chapter has considered whether a court operating within the South African constitutional parameters would be exceeding its remit and authority in interpreting the existing statutory and common law provisions in the manner proposed above and in the preceding and subsequent chapters. Setting aside normative questions such as the extent to which the state should oversee corporate actions or the accountability of company directors, this chapter considered two questions. First, whether it is constitutionally tenable for the courts to interpret the Act with such liberal reference to this extra-textual source, and second, whether a court would be justified in developing the common law with reference thereto.

The analysis has shown a well-founded reluctance on the part of the courts to interpret statutory provisions in such a manner that the autonomy of the legislature is undermined. Given the cases and historical context it seems unlikely that the code could be consulted based on it being custom. A more liberal interpretation of the decision in *Endumeni* might open the door to its introduction as either existing context or, perhaps more feasible, as part of context which speaks to the genesis of the text (although as the discussion above has shown the latter has especially been treated with circumspection by the courts in the past). In favour of this argument would be the liberal references to the code in preparatory reports that informed the drafting of

the legislation and clear references in the purposes of the Act itself that it aims to ensure good governance.

However, there are convincing arguments to the contrary. The most recent decision of the SCA on the appropriate interpretation and application of the judgement in *Endumeni* indicate that the courts will not interpret its references to context liberally and will therefore not allow extrinsic evidence to be led in order to convince the court of the proper meaning of legislative provisions.¹⁸³ The warnings that underlie the exclusionary rule that dominated English law extend to the introduction of extra-textual material which was, at the end of the day, drafted by an entity not affiliated with government that may have its own agendas and concerns and these may or may not align with national strategy and policy.¹⁸⁴

The alternative may be that the courts could develop the common law pertaining to directors' duties to take cognisance of the code. However, as the discussion has also shown, such developments will be incremental and could not introduce the sweeping policy changes that such an approach might amount to.¹⁸⁵ In the final instance, it could also be argued that the constitutional imperative that both statute and common law should reflect the spirit, purport and objects of the Bill of Rights, would justify a bolder interpretation by the courts. However, the analysis above has shown that in

¹⁸³ On a practical note, the problem becomes how the principles of the code are then to be introduced in court in the first place. They are not such that the judge could simply take judicial notice, and they may not be introduced via evidence (expert or otherwise).

¹⁸⁴ The counter argument may well be that the Institute of Directors is better placed than parliament to draft these types of rules in the first place, and in fact where such codes of conduct are mandated by legislation they are in any event often delegated to committees of unelected experts to prepare.

¹⁸⁵ This is true especially of the duty to act in the best interests of the company, where such a step might have significant impact on the state of the stakeholder debate in South African Law. In this regard cf Irene-Marie Esser & Piet Delpont 'The protection of stakeholders: The South African social and ethics committee and the United Kingdom's enlightened shareholder value approach: Part 1' (2017) *De Jure* 97, 106 who argue the opposite and are of the opinion that it in fact reflects a more reticent form of change.

both the case of the development of the common law and in the case of the interpretation of the statutory duties there are several constraints that would apply.¹⁸⁶ The implications of this analysis will be discussed more fully in chapter 8 with reference to the rest of this thesis, at which stage some final conclusions will be drawn. Before doing so, normative and policy considerations that relate to the regulation of directors and the appropriate level of accountability have to be considered.

¹⁸⁶ Consider for example the following warning: 'There lies a deeper and more troubling problem that arises from the very way in which governance reform has been effected over the past few years. Responsibility for reform has been semi-privatised, with the initiative firmly in the hands of fairly small and unrepresentative committees, championing a narrow range of interests, and apparently proceeding more on the basis of casual empiricism than well-grounded theories.' CA Riley, 'Company Law: Whither UK Corporate Governance?' (1997) 1 *Amicus Curiae* 16.

CHAPTER 6

COLLISIONS AT THE INTERSECTION – NORMATIVE DEBATES

One of the fundamental theoretical debates in economic science, directly affecting other disciplines such as law, politics and sociology, concerns the nature and role of institutions in the operation of markets. Should formal institutions, such as mandatory legal rules, be entrusted to govern economic activity or should privately negotiated governance mechanisms prevail? In other words, should the state intervene to regulate market transacting or would this impede the proper functioning of markets? And to turn to the field of corporate governance, how should corporate relationships be governed, through law or contract?¹

1 Introduction

Chapters 3, 4 and 5 of this thesis have considered the legal status of corporate governance codes and the other regulatory mechanisms in place in South Africa, with reference to the United Kingdom and other jurisdictions. In particular, the duties owed by the independent non-executive director were analysed to consider the practical impact of an inclusive interpretation drawing from voluntary codes of governance. Having also discussed the potential technical and constitutional concerns that such an approach will inevitably raise, the thesis turns now to the extent to which it is normatively appropriate for the *minutiae* of governance to be regulated by black letter law.

This is hardly a novel inquiry. As Attenborough pointed out, much ink has been spilled over the question of whether ‘conventional legal approaches or private governance arrangements are the optimal rule-making strategy to

¹ Michael Galanis ‘Vicious Spirals in Corporate Governance: Mandatory Rules for Systemic (Re)Balancing?’ (2011) 31(2) *Oxford J.Leg.St.* 327.

regulate the complexity of corporate activity'.² The sheer volume of academic work related to these topics could be a thesis of its own and no attempt will be made to engage with all the intricacies of the debate or all of the literature that has seen the light of day in attempts to explain them.³ Instead, the aim of this chapter is to offer a synthesis of the most pertinent theories and debates that speak to the appropriate and optimal regulation of corporations. Even this is an ambitious task and must be preceded by the caveat that the analysis will be limited by the boundaries of the research question.⁴

As this chapter will show, it is hardly possible to engage with the nature and proper regulation of a company without referencing developments in financial theory, and micro-economics. The impact of law and economics scholarship is such that it can almost be considered trite. And although the movement originated in the United States its theories were accepted widely and have influenced corporate law scholarship and corporate governance

² D Attenborough, 'Empirical insights into corporate contractarian theory' (2017) 37 (2) *Legal studies* 191, 191.

³ See *inter alia*: Attenborough (n2) 191; Mathew T. Bodie 'The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm' (2012) 35 *Seattle U. L. Rev.* 1033; William W. Bratton 'Self-Regulation, Normative Choice, and the Structure of Corporate Fiduciary Law' (1993) 61 *Geo. Wash. L. Rev.* 1084; BR Cheffins *Company Law: Theory, Structure and Operation* (Clarendon Press 1997); John C. Jr. Coffee 'The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role' (1989) 89 *Colum. L. Rev.* 1618; Galanis (n1) 327; Henry Hansmann & Reinier Kraakman 'The End of History for Corporate Law' (2001) 89 *GEO. L.J.* 439; Kraakman R and others *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn Oxford 2017); Marc T. Moore 'Whispering Sweet Nothings: The Limitations of Informal Conformance in UK Corporate Governance' (2009) 9 *J. Corp. L. Stud.* 95; Moore MT *Corporate Governance in the Shadow of the State* (Hart 2013).

⁴ For purposes of this chapter it must be noted that "corporate governance" will be used in both the broader sense (as in referring to any laws and regulations that have bearing on the management of internal corporate relations) and in the more narrow sense (as in referring to the corporate governance movement and those principles most typically found in voluntary governance codes). Some of the issues under consideration will apply equally to both while others are more unique to the latter.

on a global scale.⁵ Traditional ‘theories of the firm’ seek to justify the existence of the corporation, while several alternative doctrines and philosophies seek to explain the power dynamics at play within the corporation, and consider its regulation from various perspectives.⁶

The economic and financial theories specifically, provided researchers with a toolkit, through which they were able ‘to operationalize the study of corporate law “in action”, generating a wealth of new empirical insights’.⁷ It also ‘supplied a set of normative principles, derived from economic notions of efficiency, for evaluating the wealth and welfare effects of corporate law rules and doctrines’.⁸ Because of the impact these theories have had on the corporate law scholarship at issue in this chapter, the research would not do the topic justice without first considering the theoretical context of this economics driven scholarship. Attenborough gives a pointed summary of the impact of contractarian theory which emphasises its relevance for purposes of this chapter and thesis:

Overall, it is fair to suggest that the contractarian theory has permeated the theoretical discourse in US corporate legal scholarship, and inevitably influenced the academic writings of a number of UK and other Commonwealth company law textbooks and law review articles. Simultaneously, the theoretical discourse is the

⁵ Galanis (n1) 327; PM Vasudev ‘Law, Economics, and Beyond: A Case for Rethorizing the Business Corporation’ (2010) 55 McGill Law Journal 911.

⁶ Bob Tricker *Corporate Governance: Principles, Policies and Practices* (3rd edn, Oxford, 2015) 68 - 70. Tricker points out that there have been other perspectives also, such as Game theory, and theories such as those developed by Filatotchev and Wright which view corporations from a longitudinal perspective (see Igor Filatotchev & Mike Wright (eds) *The Life Cycle of Corporate Governance* (Edward Elgar 2005)). There are also perspectives from political economics such as the very well-known work of Roe who considered political and social conflict in corporations and institutions of corporate governance to show how a country’s political economy interacts with legal structures and financial markets (Mark J Roe *Political Determinants of Corporate Governance* (Oxford University Press 2003)).

⁷ Simon Deakin ‘The Corporation as Commons: Rethinking Property Rights, Governance and Sustainability in the Business Enterprise’ (2012) 37 *Queen’s L.J.* 341.

⁸ Deakin (n7) 341.

manifestation of a form of politics and it organises the political space, often with the intention of monopolising it. To this end, it has found favour in various significant policy-making discussions that go to the heart of UK company law and practice. Moreover, the rules of company law itself comprise many different elements that appear to give credence to a private contractual view of the company.⁹

A comprehensive analysis of the proper contents of a corporate law regulatory model must be conducted against the backdrop of these theoretical underpinnings. In considering these matters, this chapter will at first outline prevalent theories of the firm to give context to a more detailed analysis of agency cost theory and contractarianism – the latter being the most appropriate theories to engage with in unpacking the research questions.¹⁰ It will then explain how law and economics and financial scholarship impacted corporate law and informed its development. Following this, part 4 will turn to the core question of whether it is most appropriate for corporate governance to be formally enforced (as per Sarbanes-Oxley)¹¹ or whether voluntary codes on a comply or explain basis are more appropriate, before finally considering whether any conclusions can safely be drawn from this discussion that could shed further light on the research question. Concluding remarks will also refer to the reasons why the South African context is unique, and the specific idiosyncrasies that come into play in regulating South African companies.¹²

⁹ Attenborough (n2) 206.

¹⁰ It must be noted that the research question could be debated fruitfully with reference to other theories also. However, as these are certainly the most pervasive theories, and those that have generated the greatest body of literature they were identified as the most useful for purposes of this enquiry. See also chapter 1 for a demarcation of the thesis and research question for further comments in this regard.

¹¹ The Sarbanes-Oxley Act of 2002 available online at <https://www.congress.gov/bill/107th-congress/house-bill/3763/text>.

¹² Several tensions come to mind, such as the fact that the country is a developing economy and faces a crippling wealth disparity, high unemployment rates and battles corruption in especially the public sector. Regulators will be mindful of these pressures but also the need to attract foreign direct investment which must be

It goes without saying that this is a very ambitious scope for a single chapter and as such many of the issues will have to be considered in broader strokes and as a review of the existing literature. However, it is submitted that despite this, the analysis will have adequate depth to inform the research questions central to the thesis.

In summation, prevailing thoughts about the proper role of corporate law and regulation speak to two related debates that are most relevant to this thesis. First, as mentioned, to what extent should regulatory oversight be tolerated,¹³ and second, what is the role of corporate governance codes (and arguably other sources of perceived best practice) in such regulation. When all is said and done, the conclusion will almost inevitably be a call for balanced regulation (as it so often is). However, considering the macro challenges that society and by extension its corporate citizens now face, and the numerous complexities of business on a global scale this balance may be hard to come by. This is arguably more true in developing economies such as that of South Africa where the realities of enormous wealth disparity, and the socio-economic concerns that accompany it, inevitably puts regulators under additional pressure.¹⁴ What is more, as was shown in chapters 1 and 5, the South African legislature and judiciary undertake their tasks against

balanced against the human rights mandates contained in the constitution. See further below but see also regarding the drafting of corporate law in a developing economy: Bernard Black and Reinier Kraakman 'A Self-Enforcing Model of Corporate Law' (1996) 109(8) *HarvLRev* 1911.

¹³ This is an abbreviation of a more intricate question which has been approached from numerous angles. It could refer to the extent to which regulation should be prescriptive as opposed to facilitative, the extent to which mandatory rules should be allowed to dominate legislation, the role of so-called 'opt out' provisions and the extent to which matters related to such regulation should be enforced by the judiciary or formal process. Without attempting to simplify the matter and paint all these issues with the same brush, the thesis will attempt to distil the relevant and overarching principals from the appropriate research in order to relate them to the questions at the heart of the research.

¹⁴ See note chapter 7 text to note 41.

the backdrop of a dynamic constitutional mandate, adding another layer to a panoply of issues.

2 Theories of the Firm: A General Overview

Economists were in no immediate hurry to justify the existence of the firm¹⁵ or engage with its inner dynamics, choosing instead to refer to it as a black box taking in inputs and putting out outputs.¹⁶ As Williamson would note, this is perhaps because 'it is much easier to say that organization matters than it is to show how and why.'¹⁷ In fact even Jensen and Mecklin acknowledged that '[i]t is embarrassing to admit that, after several hundred years, social scientists have not yet developed a thorough understanding of the advantages and disadvantages of publicly held profit seeking corporations versus other forms of organizations such as cooperatives, nonprofit corporations, universities, proprietorships, joint ventures and mutuals.'¹⁸

With his article *The Nature of the Firm*,¹⁹ Coase famously took the first peek inside the box and tried to address why the firm prevailed over a system that relies merely on markets and contracts.²⁰ In a nutshell, Coase finds

¹⁵ John Kay 'Theories of the Firm' (2018) 25(1) *Int. J. Econ. Bus.* 11; Deakin (n7) 350 on the distinction between 'firm' as used in this sense in economic theory and 'corporation' or 'company' as a legal term.

¹⁶ Bodie (n3) 1040. For an analysis of how the concept of a black box is used to theorise in this manner, and an overview of economic theorists that used it see Alice Belcher 'Inside the Black Box: Corporate Laws and Theories' (2003) 12(3) *Social and Legal Studies* 360.

¹⁷ Oliver E Williamson 'The Theory of the Firm as Governance Structure: From Choice to Contract' (2002) 16(3) *JEP* 171.

¹⁸ Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 *J. Financ. Econ.* 30.

¹⁹ Ronald H Coase 'The Nature of the Firm' (1937) 4(16) *Economica* 386.

²⁰ Coase was awarded the Nobel Prize in Economic Sciences for "for his discovery and clarification of the significance of transaction costs and property rights for the institutional structure and functioning of the economy" and his important contributions on the borderline between economics, law and organization. See: The Nobel Prize: Ronald H Coase, available online at: <https://www.nobelprize.org/prizes/economic-sciences/1991/coase/facts/>. And

justification for the firm in transaction cost economics. Although price movements could direct production even in the absence of the firm, the latter can avoid the transaction costs created through market organisation.²¹ It was especially the ability of the firm to manage workers that reduced these costs,²² as '[t]he boundaries of the firm were defined by the relative costs of two methods of co-ordination: markets and the price mechanism versus central direction and management hierarchies.'²³

Coase's model was developed further by Oliver Williamson who expounded on the challenges that would favour firm governance as opposed to the use of market mechanisms.²⁴ Williamson contended that the savings achieved by avoiding the market would only hold until the firm reached a critical size, at which stage the governance structure that the company chose could overcome the disadvantages of scale. In short, this leads transaction cost economics to focus 'on the cost of enforcement or check-and-balance mechanisms, such as internal and external audit controls, information disclosure, independent outside directors, the separation of board chairmanship from CEO, risk analysis, and audit, nomination and

see: Robert Higgs 'Ronald Coase, Anomalous Superstar of the Economics Profession' (2014) 19(2) *The Independent Review* 309; Robert Hahn 'Ronald Harry Coase (1910 – 2013): Nobel-prizewinning economist whose work inspired cap-and-trade' (2013) 502 *Nature* 449.

²¹ Vasudev (n5) 915.

²² Coase (n19) 386. And see: Bodie (n3) 1040; Kay (n15) 11.

²³ Kay (n15) 11.

²⁴ Oliver E Williamson *The Economic Institutions of Capitalism: Firms, Markets, Relational Contracting* (1985 Macmillan). Bodie offers a further useful if brief summary of his thesis: "When contributions and compensation are harder to value individually, the parties will be left with incomplete and ambiguous contracts. And these contracts will be insufficient to properly allocate economic power within the relationship particularly where one or both of the parties must invest significant resources in assets specific to the particular firm, project, or transaction. In order to prevent opportunism in the face of these contracts, some system of governance is necessary to deal with ex ante developments. Firms can provide this governance. By creating legal structures that allocate control between the parties separate and apart from their contractual rights, governments can assist parties in developing relationships that minimize transaction costs and facilitate economic growth." See: Bodie (n3)1041 – 1042.

remuneration committees. The argument is then advanced that such enforcement costs should be incurred to the point at which the increase in costs equals the reduction of the potential loss from non-compliance.²⁵

After a hesitant start, scholars were enthusiastically poking around in the black box by the 1970's, expounding on existing theories and developing new ones.²⁶ It was Jensen and Meckling (in 1976)²⁷ and Easterbrook and Fischel (in 1984²⁸) who finally 'coined' the firm as a 'nexus of contracts'.²⁹ Thus, from an economic perspective the firm stood 'at the centre of a web of legal agreements, with employees, suppliers, customers, and lenders.'³⁰ And yet, especially if considered from the vantage point of the shareholder, it is clear that these legal agreements could never adequately cope with any and all eventualities. A great deal of the contracted relationship remains implied, and while the courts are of course able to enforce implied terms, they identified hierarchy as the force that keeps most of the corporate cogs turning.³¹

²⁵ Tricker (n6) 65.

²⁶ Several sources offer comprehensive accounts of these theories and how they have impacted corporate law. See for example: Philippe Aghion and Richard Holden 'Incomplete Contracts and the Theory of the Firm: What Have We Learned over the Past 25 Years?' (2011) 25(2) *JEP* 181; Alice Belcher 'The Boundaries of the Firm: The Theories of Coase, Knight and Weitzman' (1997) 17 *JLS* 22; Belcher 'Inside the Black Box' (n16) 359; Deakin (n7) 339; Andrew S. Gold 'Theories of the Firm and Judicial Uncertainty' (2012) 35 *Seattle U.L.Rev.* 1087; Kay (n15) 11; Eric W. Orts 'Shirking and Sharking: A Legal Theory of the Firm' (1998) 16 *YALE L. & POL'Y REV.* 265; Vasudev (n5) 911; Williamson 'The Theory of the Firm as Governance Structure' (n17) 171.

²⁷ Jensen and Meckling (n18) 305.

²⁸ Easterbrook Frank H & Fischel Daniel R 'The Corporate Contract' (1984) 89 *Col.L.R* 1416.

²⁹ Kay (n15) 12 where the author points out that this idea "had been present from the very beginnings of the modern corporation in the legal doctrine of corporate personality – people dealing with the firm transacted with a corporate entity, not the individuals who represented the organisation."

³⁰ Kay (n15) 12.

³¹ Kay (n15) 12.

This ideology prompted the well-known ‘property rights theory’ developed mainly by Sanford Grossman, Oliver Hart, and John Moore.³² These authors ‘identified the “owner” within the nexus of contracts as the person who determines the indeterminate elements of inevitably incomplete contracts.’³³ The shareholders, residual claimants to revenues and assets, and at least in theory collectively possessed of the power to enforce their will, fulfilled this role of arbitrators of whatever was not spelled out contractually.³⁴ This hypothesis in turn led to the development of principal agent problem as ‘the central issue of organisational design’.³⁵ Jensen and Meckling’s 1976 article,³⁶ which set out how incentive schemes might serve to align the interests of the managers (agents) with the objectives of the organisation (and indirectly the shareholders), proved incredibly influential.³⁷ What finally heralded the era of ‘shareholder value’³⁸ was Milton Friedman’s article in the *New York Times*, cited so often that the title would later become a ubiquitous ‘call to arms’: ‘The Social Responsibility of Business is to Maximise Profits.’³⁹

³² Oliver Hart & John Moore ‘Incomplete Contracts and Renegotiation’ (1988) 56(4) *Econometrica* 755; Sanford J. Grossman and Oliver D. Hart ‘The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration’ (1986) 94(4) *JPE* 691. The theory was developed in a series of articles by the authors and was in fact so highly regarded that it resulted in the Nobel Prize (Economic Sciences) for Oliver Hart in 2016: *The Nobel Prize: Oliver Hart* at <https://www.nobelprize.org/prizes/economic-sciences/2016/hart/biographical/>; and see Richard Holden ‘A Nobel Prize for Property Rights Theory’ (2017) *Games* 4; Aghion and Holden (n26) 181.

³³ Kay (n15) 12. And see Bodie (n3)1042 where the author explains how the theory considered the firm as “a repository of property rights for assets used in joint production” and requires that those who contribute “the most valuable and most asset-specific” property to the enterprise should own the firm.

³⁴ Kay (n15) 13.

³⁵ Kay (n15) 13.

³⁶ Jensen and Meckling (n18) 305.

³⁷ As Kay points out, this was no doubt due to the fact that the argument was congenial to executive managers themselves. Kay (n15) 13.

³⁸ See also discussion of ‘shareholder value’ in chapter 4.

³⁹ As cited by Kay (n15) 13: Friedman, Milton. 1970. “The Social Responsibility of Business is to Maximise Its Profits.” <http://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html>

The narrative thus far, highlights the mainstream theories that gained the widest acceptance by the academy, business and practitioners and eventually matured to become the agency costs and nexus of contracts theories long seen to support a shareholder primacy approach to corporate law. There were alternative approaches besides these, such as the ‘team production theory’ proposed by Alchain and Demsetz,⁴⁰ which explained the firm ‘as a way of pooling disparate inputs into a system of cooperative creation’.⁴¹ Subsequent macro-economic shifts from manufacturing toward services prompted the development of a theory based on human capital and referred to as the ‘knowledge-based’ theory of the firm.⁴² The focus here moved away from the ownership of physical assets and instead turned to ‘the need to produce, distribute, and ultimately retain valuable knowledge-based assets within the firm’.⁴³ Resource dependency theory in its turn, took a more strategic view of corporate governance. Although it did not gain much ground when first presented, Kay argued recently that it may well be the theory best positioned to assess the modern corporation.⁴⁴ It views directors as ‘boundary-spanning nodes of networks able to connect the business to its strategic environment...’ and recognises the fact that the social networks that link those involved in the governance process can enhance or hinder governance activities.⁴⁵

⁴⁰ Armen A. Alchain and Harold Demsetz ‘Production, Information Costs, and Economic Organization’ (1972) 62(5) *AER* 777. Firms can synchronise production between different groups without having to divide these various relationships up to govern them through distinct contracts. Such a ‘team method’ increases productivity, but the most obvious pitfall is the fact that any member of the team might shirk his or her responsibilities. Bodie (n3)1041

⁴¹ Bodie (n3) 1041. The theory then sees the firm itself serving as a central monitor to ensure that each member makes an appropriate contribution and is compensated proportionally.

⁴² Bodie (n3) 1043.

⁴³ Bodie (n3) 1043.

⁴⁴ Kay (n15) 13.

⁴⁵ Tricker (n6) 68.

Of the remaining paradigms, three final propositions are worth mentioning in brief. The first of these, stewardship theory, can perhaps be described as the ‘antithesis’ to agency theory. Proponents focus on the resilience and success of the original form and function of the joint stock company. This original system, which sees managers being authorised to act as stewards, subject to reporting requirements and fiduciary duties that serve as safeguards, is considered essentially sound. At its core, stewardship theory reflects the ‘classic ideas of corporate governance’ and essentially believes that directors are to be trusted. Although some directors will fail, the argument goes, this does not undermine the basic construct or imply that directors are necessarily self-serving or unable to act with integrity and independence.⁴⁶

Critics of the stewardship theory emphasise that we have come some way since the 19th century model of the company first saw the light of day. Structures are now far more complex, and transparency and accountability cannot be taken for granted.⁴⁷ A further criticism is the normative nature of the theory. It “emphasizes what should be done, or even exhorts” and is therefore not predictive in nature and unable to show causality between any behaviour and corporate performance.⁴⁸ Perhaps more importantly, collapses on the scale of Enron and the 2008 financial crisis left many disillusioned and with a sense that the trust that the stewardship model extends to directors had been betrayed with dire consequences for stakeholders. This led many to call for a redress in the balance of power, and for the greater empowerment of shareholders. Indeed, following the financial crisis shareholder enfranchisement was one of the primary manners in which regulators tended to respond.⁴⁹

⁴⁶ Tricker (n6) 65.

⁴⁷ Tricker (n6) 66.

⁴⁸ Tricker (n6) 66.

⁴⁹ See for example: “However, sceptics of shareholder empowerment have argued that boards, elected by investors, should still have primacy. Only the directors are

The following discussion will illustrate how economic theory was assimilated by corporate law theorists and debate its continuing role in shaping the discourse that speaks to this area of the law.

3 Finance, Firm, and Takeover Mania: A Revolution and its Consequences

a. Chronology

Corporate law in the 1960's (at least in the United States) was described as 'ossified, stagnant'⁵⁰ and dead 'as a field of intellectual effort'.⁵¹ Not short on dramatic flair, Bayless Manning lamented that '[w]e have nothing left but our great empty corporation statutes – towering skyscrapers or rusted girders, internally welded together and containing nothing but wind.'⁵²

A relief then, that the 1970's and 1980's brought about a paradigm shift in corporate law scholarship. Termed a 'revolution' by some,⁵³ its impact was

in a position to take into account relevant factors in business decisions. Giving more power to investors...would increase investor costs and reduce returns". Tricker (n6) 66.

⁵⁰ Romano R 'After the Revolution in Corporate Law' (2005) 55 *Journal of Legal Education* 343. And see: William Carney 'The Legacy of the "Market for Corporate Control" and the Origins of the Theory of the Firm' (1999) 50 *Case Western Reserve Law Review* 221-225.

⁵¹ Bayless Manning 'The Shareholders' Appraisal Remedy: An Essay for Frank Coker' (1962) 72 *Yale L.J.* 245 n.37.

⁵² Later to become Dean of Stanford Law School. See: Bayless Manning 'The Shareholders' Appraisal Remedy: An Essay for Frank Coker' (1962) 72 *Yale L.J.* 245 n.37.

⁵³ Bodie (n3) 1033; Orts (n26) 265. And see Romano R 'After the Revolution in Corporate Law' (2005) 55 *Journal of Legal Education* 342, where the author offers a comprehensive chronicle of the changes, remarking that: "Corporate law is a field that underwent as thorough a revolution in the 1980s as can be imagined, in scholarship and practice, methodology and organization. The term "revolution" is invoked all too often in popular culture, but ... it is entirely apt in this case. The revolution in corporate law has been so thorough and profound that those working in the field today would have considerable difficulty recognizing what it was

such that once the dust had settled, authors Hansmann and Kraakman announced the ‘end of history for corporate law’,⁵⁴ arguing that we had now more or less reached international agreement on the basic structures and principles that underpin the corporation.⁵⁵

The agent of this revolution was the emerging methodology of law and economics which, the story goes, turned corporate law academia from ‘a swampy doctrinal backwater’ into a ‘vibrant hub of intellectual activity’ by introducing such concepts as agency costs, shareholder primacy, and the market for corporate control.⁵⁶ These ideas are now so entrenched that one can hardly discuss the regulation of corporations without at least a nod in their direction.⁵⁷ Law and economics scholars soon took for granted that their audience arrived well versed in the basics of this new scholarship – even to the point that they tended to avoid discussing more general principles and turned directly to finer details and more contentious arguments.⁵⁸

Romano traces the origins of this “new paradigm for corporate law” back to the work of Henry Manne,⁵⁹ who was the first to recognise the merger as

twenty-five to thirty years ago.” (at 342). And see: Cheffins (n3) v, where the author prefers more reticent language but nonetheless confirms that ‘[c]ompany law [had] undergone an academic transformation...’

⁵⁴ Hansmann and Kraakman (n3) 439.

⁵⁵ Hansmann and Kraakman (n3) 439.

⁵⁶ Bodie (n3) 1033. And see Cheffins (n3) v: “[a] rich theoretical literature has developed in law reviews and related journals, with the use of economic analysis providing much of the impetus for this work.”

⁵⁷ Bodie (n3) 1033. Most notable publications on Company Law will have one reference or another to at least some, if not all, of these issues.

⁵⁸ So prevalent was this practice that by 1997 Cheffins observed that the emerging body of learning remained inaccessible to scholars and set out to address this in a comprehensive analysis of background principles. See: Cheffins (n3) v.

⁵⁹ Henry G Manne ‘Mergers and the Market for Corporate Control’ (1965) 73 *J. Pol. Econ.* 110

something more than merely a threat to competition.⁶⁰ Shortly thereafter, Ralph Winter came to conclusions along similar lines.⁶¹ Both authors were largely ignored by the academy at the time, who viewed corporate law as essentially a species of consumer protection, and supported the adoption of a national corporation law in America to ensure adequate protection for investors.⁶²

In a useful chronology of the developments, Romano identifies three strands that did eventually lead to a transformation of corporate law.⁶³ The first is the emergence of corporate finance as a serious field of study in the latter half of the twentieth century.⁶⁴ The second is a parallel development in microeconomics which heralded a new theory of the firm – in particular transaction cost economics and the agency costs theory of the firm.⁶⁵ Finally, radical changes in corporate practice and the ‘era of the hostile takeover’ which spurred an ‘explosion in innovative deals’.⁶⁶ The fast paced, takeover

⁶⁰ Manne was also the first to engage with the concept of market control and to identify the potential of the merger and the takeover to enhance efficiency by replacing mediocre management. Romano (n53) 343; Manne (n59) 110.

⁶¹ Winter R K ‘State Law, Shareholder Protection, and the Theory of the Corporation’ (1977) 6 *J.Leg. Stud.* 251. Winter argued against the prevailing perception that American states would legislate in a race to the bottom and offer investors as little protection as possible, noting that directors would be dissuaded from operating in such states.

⁶² Romano (n53) 344.

⁶³ Romano (n53) 345.

⁶⁴ The field of corporate finance was first considered as an influence on corporate law by Victor Brudney and Marvin Chirelstein in a ground-breaking case book published in 1972 (Victor Brudney and Marvin A Chirelstein *Cases and Materials on Corporate Finance* (Mineola 1972)). See: Romano (n53) 345. The author sets out a chronology of the breakthroughs in finance which in turn enabled the evolution of corporate law. Among others, she points to the emergence of event studies, developed together with the concept of market efficiency and able to test finance theory and the theories proposed by Manne and Winter.

⁶⁵ These theories were the result of economists’ attempts to decipher the ‘black box of the firm’ as neo-classical economics focussed on the firm as a production function, termed it. Romano (n53) 347. And see further below.

⁶⁶ Romano (n53) 347. For a further review of the ‘Takeover Wave’ of the 1980’s, see also: Andrei Shleifer and Robert W. Vishny ‘The Takeover Wave of the 1980s’ (1990) 249 *Science, New Series* 745.

driven scene of the 1980's forced lawyers to work increasingly together with the investment banking sector, and although they did not always welcome this fact, there was simply no choice but to become 'increasingly conversant' in finance and economics. The courts and the U.S Securities and Exchange Commission followed suit, and also drew from developing financial theories in formulating legal rules.⁶⁷ The concepts transposed from institutional economics were used to generate a 'functional'⁶⁸ theory of corporate law 'which promised to uncover the economic structure of the legal rules governing the firm.'⁶⁹ Where lawyers and the courts had found themselves floundering when talking and thinking about the consequences of the novel transactions that they were encountering, 'the theoretical developments in finance and in the theory of the firm literature provided the language and analytical tools to address a host of challenging legal issues.'⁷⁰ Deakin explains that it was essentially a reductive process that saw an inevitable development from contractarian theory to the structure of the firm being based on agency conflict, noting that '[a]lmost the entirety of the modern economics-inspired tradition of corporate law scholarship is derived from this methodological move, which is so generally accepted as to be almost taken for granted'.⁷¹

And so, corporate law scholarship seemed to greet the new millennium *ad idem* about the fact that the norm of shareholder primacy had prevailed (due largely to the efficiency gains it ostensibly generated), and corporate

⁶⁷ This was an era of creative deals and transactions and colourful terminology such as 'crown jewels', 'white knights', 'poison pills' and 'greenmail'. The trend would prevail in spite of numerous attempts by the legislature in the United States to curtail it. Romano (n53) 350. And see: Deakin (n7) 340.

⁶⁸ First used by Hansmann and Kraakman to describe corporate law as informed by economic theory. See: Henry Hansmann & Reinier Kraakman, "What is Corporate Law?" in Reiner Kraakman et al, eds, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (Oxford: Oxford University Press, 2004) 5.

⁶⁹ Deakin (n7) 340.

⁷⁰ Romano (n53) 347. And see: Deakin (n7) 341.

⁷¹ Deakin (n7) 344.

law and practice would merge along these lines (prompting the abovementioned article by Hansmann and Kraakman heralding the end of corporate law).⁷² Deakin argued that this prediction has since proven false because of resistance of national systems to the convergence of corporate governance rules but also because of the fact that the global financial crisis was such a shock to the universal system.⁷³

The financial crisis of 2007/2008 did more than to destabilise the global economy. It shook established notions about corporate law and prompted scholars to question the accepted theories of the firm that had informed and shaped corporate law regulation and jurisprudence. Where there had been a wholesale acceptance of the idea that company law should become increasingly enabling and is there merely to facilitate an existing 'nexus of contracts', scholars were now considering theories of the firm from new perspectives.⁷⁴

Thus, although the shareholder primacy model which had become the dominant legal-economic theory at the turn of the century had to be reconsidered, this did not imply a general rejection of economic theory or the social sciences when analysing and researching legal norms.⁷⁵

When it comes to the role of economic theory or the social sciences in generating and interpreting corporate law, Gold made the observation that there is no necessary connection between theories of the firm scholarship and judicial theories of the firm. He argued that is no surprise that

⁷² Deakin (n7) 341 in reference to the famous article by Hansmann and Kraakman (n3) 439.

⁷³ Deakin (n7) 342, where the author points out evidence suggesting that "firms characterized by a higher degree of shareholder influence over managerial decision making ... were more exposed to risk in the run-up to the crisis and more likely to fail during it." And see Bodie (n3) 1039; Jill E. Fisch 'Measuring Efficiency in Corporate Law: The Role of Shareholder Primacy' (2006) 31 *J. CORP. L.* 638. See also regarding shareholder primacy chapter 4 at note 86 and further and sources cited.

⁷⁴ Deakin (n7) 342.

⁷⁵ Deakin (n7) 343. And see: Bodie (n3) 1045; Fisch (n73) 638.

economists and legal scholars might adopt a particular theory of the firm while the courts opt to endorse another: judges are not economists and not positioned to keep abreast of the increasingly sophisticated theories of the firm that are so rapidly emerging.⁷⁶ He explained that '[l]egal scholars who focus on theories of the firm often develop an interpretation of corporate law that endorses a particular legal theory of the firm. On these accounts, courts are thought to have adopted a commentator's preferred theory (consciously or otherwise), with legal doctrine seen as a means of facilitating the formation and governance of firms with the desired features.'⁷⁷ He argued however, that corporate law can be considered from a different viewpoint, and that much of corporate legal doctrine is in fact a reaction to uncertainty among the judiciary as to the appropriate theory of the firm as opposed to an endorsement of any one particular theory.⁷⁸

There is merit in the argument. However, this it does not negate the pervasive influence of these theories in how regulators and the judiciary perceive company law. As Moore pointed out, contractarianism is manifested in how the judiciary in both the UK and the US approach cases in corporate law.⁷⁹ He pointed to a long tradition of judicial deference to the internal contractual autonomy of corporations in the United States (entrenched by the operation of the common law business judgement rule), and judicial deference to internal corporate autonomy which 'persists in the English common law environment under the doctrinal label of the 'internal management' doctrine'.⁸⁰ Arguably judges may not consciously favour any

⁷⁶ Gold (n26) 1087.

⁷⁷ Gold (n26) 1087.

⁷⁸ Gold notes that "[t]here is also evidence in support of this hypothesis. Courts, in fact, seem to go out of their way to avoid adopting a particular theory of the firm. At the same time, actual case outcomes are subject to multiple interpretations from a theory of the firm perspective. Moreover, leading explanatory theories often must identify at least some cases as exceptions to the rule, a necessity that indicates these theories do not perfectly fit the case law." Gold (n26) 1087.

⁷⁹ Moore *Governance in the Shadow* (n3) 1.

⁸⁰ Moore *Governance in the Shadow* (n3) 8.

one theory over another, but the existing legal paradigm, its jurisprudence and preceding case law may have endorsed contractarianism to the extent that there is no escaping its influence.

It is also apparent that the legislative approach in both the United States and the United Kingdom has been shaped by the ideologies underpinning contractarianism. As noted above, ‘the contractarian paradigm is dependent on a peculiarly passive-instrumentalist understanding of corporate law as a phenomenon that is in the last place *determined by*, rather than determinative of, the private preferences and bargains of individual corporate participants (principally shareholders and managers)’.⁸¹ The influence of this logic on legislative approach is evident in US corporate governance in the ‘opt-out’ traditions of State corporate governance design. In the UK it is demonstrated most conspicuously in the significant degree of regulatory deference apparently afforded to so-called ‘soft law’ norms that are promulgated outside of government and which depend mainly on market pressures, rather than the binding force of state sanction, for their effectiveness in eliciting managerial behavioural change’.⁸²

One can make a convincing argument that the regulatory regime in South Africa shows similar influences. The 2008 Companies Act expressly favours a ‘facilitative’ approach and includes numerous ‘opt in/opt out’ type provisions throughout.⁸³ Furthermore, as mentioned in previous chapters, corporate governance is regulated via soft law norms as is the case in the United Kingdom. The South African courts in large part endorsed their English and American counterparts’ reluctance to interfere in internal

⁸¹ Moore *Governance in the Shadow* (n3) 7. See also: Attenborough (n2) 206. The approach aligns with one based on ‘negotiated regulation’: See: Dignam A ‘Exporting corporate governance: U.K. regulatory systems in a global economy’ (2000) 21(3) *Co Law* 70 and discussion in chapter 7 at note and further.

⁸² Moore *Governance in the Shadow* (n3) 7.

⁸³ These are referred to as so-called ‘alterable provisions’ of the Act. See also discussion of alterable and unalterable provisions in chapter 1.

matters, and it is likely that the business judgement rule incorporated into the 2008 legislation will perpetuate this in many cases.

b. Agency Costs Theory

As the discussion above has detailed, certain theories of the firm had become very popular in corporate law debates by the turn of the century. Foremost was the agency costs theory and the concomitant idea of the company as a 'nexus of contracts'.⁸⁴ As mentioned in chapter 1, the agency theory refers in general to the inevitable conflicts of interests that will arise when one party has the task of furthering the interests of another. In any such situation, it is argued, the 'agent' will be inclined not to further the interests of the principal exclusively and the former must be incentivised or motivated not to act in a self-serving manner.⁸⁵ As with transaction cost theory, agency theory is rooted in financial economics, is concerned with managerial discretion, and is based on the assumption that managers are prone to opportunism.⁸⁶ At its core, the model firm is conceived of as a 'cascade of principal-agent problems'. This, according to Kay, 'was the logical culmination of what had earlier been described (though with a degree of scepticism which had increased over time) as 'scientific management'. Shareholders-owners, too busy and too numerous to manage the business themselves, contract with executives to run the business.⁸⁷

⁸⁴ See below at text to note 103 and further and sources cited.

⁸⁵ Early proponents of agency theory, Jensen and Meckling, defined it as follows: '[A]gency theory involves a contract under which one or more persons (the shareholders) engage other persons (the directors) to perform some service on their behalf which includes delegating some decision-making authority to the agent. If both parties to the relationship are utility maximizers there is good reason to believe the agent will not always act in the best interests of the principal': Jensen and Meckling (n18) 308.

⁸⁶ Tricker (n6) 65. In fact, this is the case to the extent that Bodie argues that contractarianism is no separate theory at all but instead merely an answer to the cost dilemmas identified by agency theory.

⁸⁷ Kay (n15) 13. He then defines these executive functions to include 'determination of the appropriate scope of the firm, integrating idiosyncratic activities within the

It bears mention that agency costs, and the agency dilemma is not a brand-new concept. Vasudev explains that Jensen and Meckling essentially 'adopted Ronald Coase's ideas on microeconomic theory, along with those of Adam Smith, and Berle and Means on corporate governance, and wove them together into their own theory. In Jensen and Meckling's model, Coase's entrepreneur-coordinator, rechristened as an "owner-manager", sells a part of the equity or ownership to outside investors. Jensen and Meckling's theory is therefore about business enterprises in the corporate form.'⁸⁸ Smith, of course, was mainly concerned with conflicts between shareholders as contributors of capital, and directors as controllers – he believed a conflict between the two was expected and unavoidable. Berle and Means in turn applied essentially the same principle but framed it in political terms to speak more directly to the large industrial companies that had come to the fore in the US.⁸⁹

At first glance it appears that the agency dilemma in the context of the modern public company manifests in a rather straightforward manner, with the shareholders cast as the principals and the directors as the agents managing the entity on their behalf. But the agency relationships at play in companies today are usually far more complex. As Tricker points out, where one is dealing with minority shareholders, institutional investors and block shareholders, executive and non-executive directors, and powerful creditors it becomes exceedingly difficult to trace the so-called 'agency chain' and determine where and how the company and its constituents are exposed to agency risks is almost impossible.⁹⁰ The world has come a long way from the

overall common organisational structure, and contracting in competitive markets where there are multiple potential suppliers of homogenous inputs.'

⁸⁸ Vasudev (n5) 916.

⁸⁹ Vasudev (n5) 916: 'Berle and Means framed the issue in more explicitly political terms: the concentration of power in the corporate boards and the undermining of the property rights of large numbers of retail shareholders who were understood as the "owners" of the corporations.'

⁹⁰ Tricker (n6) 60.

original idea of the joint-stock company – and it is now possible, for example, to acquire voting rights in a company without owning any shares. Directors are faced with novel dilemmas, such as whether they represent the interests of the traditional long-term shareholder, or conversely whether they steward the interests of short-term activist institutions. It is unlikely that these interests will align.⁹¹

The strength of agency theory lies in its use of data about governance practice and company performance that is easily accessible (such as directors' reports or audited company accounts), and which in turn allows for a 'statistically rigorous insight'⁹² into corporate governance practices. Its simplicity and the fact that it relies on available and reliable data and accepted statistical analysis means that agency theory has been able to make a dynamic contribution to corporate governance theory.⁹³

In addition, it is probably no surprise that the agency theory has become such a popular lens through which to view corporate governance practices and behaviours. There is hardly a dearth of anecdotal evidence to support the fact that directors have often treated listed companies as their own property, and have exploited their positions to great personal gain – often taking benefits unrelated to performance or by simply appropriating unsanctioned funds to the great detriment of the company and its shareholders.⁹⁴

⁹¹ Tricker (n6) 60, where the author points out that the agency problem is certainly not limited to relationships within listed companies, and can occur in private companies, private companies, joint ventures, not-for-profit organizations, professional institutions, and governmental bodies, not to mention a group company context, where '[t]he opportunities for the subsidiary company directors to take decisions beneficial to the subsidiary, but detrimental to the group, are legion...'

⁹² Tricker (n6) 62.

⁹³ Tricker (n6) 62.

⁹⁴ Tricker (n6) 62.

Amongst other things, this is to do with asymmetrical access to information and the fact that the directors not only have more information than the shareholders, but also (within the confines of legal requirements) curate the information that the shareholders are given.⁹⁵ At the core of the joint-stock, limited-liability company is the stewardship role of the directors, who are trusted by the shareholders to manage their contributions in the face of this asymmetry. Agency theory, in essence, takes a more sceptical view of this arrangement.⁹⁶ Kay offers a concise summary of this phenomenon:

Internal organisation requires decentralisation to those who hold the diffuse information required for efficient production while incentivising them to use that information for the advantage of the firm rather than the holder of the information. The incompleteness of contracts requires that those with superior access to information are given appropriate incentives to internalise the objective of the firm – the maximisation of value for its shareholders. A suite of models of these kinds provides a rationalist and reductive account of the role and functions of the firm which is still pervasive.⁹⁷

Despite being such a ubiquitous model, the theory faces a number of criticisms.⁹⁸ It is criticised for having a relatively narrow theoretical scope. It focusses purely on measurable data such as how the board is structured, what remuneration packages look like or how a company has complied with a corporate governance index by means of ‘box ticking’. The criticism is

⁹⁵ Somewhat ironically, this same problem arises as between the executive and non-executive directors and has been identified as one of the hurdles preventing the latter from performing their functions optimally. See chapter 4 for a general discussion in this regard.

⁹⁶ Tricker (n6) 62.

⁹⁷ Kay J ‘Theories of the Firm’ (2018) 25(1) *International Journal of the Economics of Business* 13.

⁹⁸ See for example: Paddy Ireland, ‘Property and contract in contemporary corporate theory’ (2003) 23(3) *LS* 453; William Bratton, ‘The “Nexus-of Contracts” Corporation: A Critical Appraisal’ (1989) 74 *Cornell L.Rev.* 407.

mainly that board behaviour is influenced by more than a set of contractual relationships but rather is also swayed by 'interpersonal behaviour, group dynamics and other political intrigues and question whether the subtle and complex dynamics of board behaviour lend themselves to measurement and numerical analysis'.⁹⁹ Others have criticised the very simplicity that is considered to be the model's strength, contending that some investors behave more like 'corporate raiders' than the more traditional long-term investors envisaged by the model, while the short termism that dominates stock markets may well produce different agency relationships entirely.¹⁰⁰ Yet others have challenged the findings of agency theoretical research and have concluded that the number of well-connected executive directors forming part of the company's board is a better predictor of how well the company will perform than whether or not the company followed corporate governance codes or whether it had effective independent director oversight in place.¹⁰¹

Finally, there is also the fact that agency theory is essentially rather cynical.

As Tricker puts it:

[I]nherent in agency theory is a philosophical, moral assumption about the nature of man. The theory assumes that people are self-interested, not altruistic; they cannot be expected to look after the interests of others. In other words, directors cannot be trusted. The legal concept of the corporation, and the basis of stewardship theory ... takes the opposite view.¹⁰²

⁹⁹ Tricker (n6) 63.

¹⁰⁰ Tricker (n6) 63.

¹⁰¹ Tricker (n6) 63.

¹⁰² Tricker (n6) 63. And see: Timothy L Fort and James J Noone 'Banded Contracts, Mediating Institutions, and Corporate Governance: A Naturalist Analysis of Contractual Theories of the Firm' (1999) 62(3) *Law and Contemporary Problems* 165.

c. Nexus-of-Contracts Theory

Also called ‘contractarianism’, the nexus-of-contracts constitutes ‘an economic paradigm that regards the company, and the rules related thereto, as no more than an explicit and implicit set of ‘private’ contractual arrangements between shareholders, directors, employees, creditors, suppliers, etc.’¹⁰³ Attenborough describes it as a ‘deregulatory, individualistic depiction of company law and corporate governance’, which explains the legal governance structure of the company ‘as the endogenous outcome of a collection of autonomous and rational actors freely negotiating notional bargains to produce and enforce rules that regulate their exchange activities.’¹⁰⁴

Or according to Moore, it is a theory which determines that ‘the core and motivating purpose of corporate governance laws should be to reflect or “mimic” the governance “terms” that shareholders and managers would be inclined to agree upon with one another privately, in the hypothetical scenario where no antecedent laws exist and therefore all norms stand to be determined by private negotiation alone.’¹⁰⁵ This is due to the fact that, at least in the Anglo-American context, the efficacy of laws and regulations in the corporate sphere depends on how well the rules respond to the needs of key participants or parties to the corporate contract.¹⁰⁶ It speaks to an approach that views corporate governance law as being at its core ‘organic’ or (‘bottom up’) as opposed to ‘synthetic’ or (top down),¹⁰⁷ and sees corporate law as an aspect of private or facilitative law as opposed to public law which tends to be more prescriptive. Moore points out that unlike criminal, environmental, tort and securities law, ‘corporate law – including

¹⁰³ Attenborough (n2) 192.

¹⁰⁴ Attenborough (n2) 192.

¹⁰⁵ Moore *Governance in the Shadow* (n3) 2.

¹⁰⁶ Moore *Governance in the Shadow* (n3) 2.

¹⁰⁷ Moore *Governance in the Shadow* (n3) 4.

corporate governance law – is typically not perceived as being designed to coerce social-behavioural change, or to bring about direct distributional outcomes within society whether in terms of risk, power or wealth.¹⁰⁸ He describes the laws and norms in the field of corporate governance as ‘fundamentally non-socially-determinative’ in nature.¹⁰⁹

The distinction is critically important. If one adheres to a school of thought that views corporate law as essentially private, one is likely to argue that the law should ‘respond to private preferences as opposed to determining them.’ If, however, one perceives corporate governance laws as inherently public, the normative position you are more likely to take is one that would allow for laws to ‘be coercive and socially determinative, aimed at eliciting direct change in the behavioural patterns and relative resources of key corporate participants in line with general democratic opinion in society, and irrespective of whether or not such regulatory outcomes are consistent with the affected participants’ (especially shareholders’) private preferences.’¹¹⁰

Despite the fact that it was so widely accepted, contractarianism has many critics. Belcher argues that the theory is based on ‘individual economic agents who act and make contracts in a rational way and in their own interest’.¹¹¹ Relying on work by Snider,¹¹² she contends that the theory reflects the ‘sleek, minimalist view of “Chicago-style” economics’ and

¹⁰⁸ Moore *Governance in the Shadow* (n3) 3.

¹⁰⁹ Moore *Governance in the Shadow* (n3) 3.

¹¹⁰ Moore *Governance in the Shadow* (n3) 4. And see: D Millon ‘New Directions in Corporate Law: Communitarians, Contractarians, and the Crisis in Corporate Law’ (1993) 50 *Wash. & Lee L. Rev.* 1373. And see Bodie (n3) 1047: ‘because a corporation is merely an intersection of voluntary agreements, corporate law should facilitate freedom of contract and eschew mandatory rules.’

¹¹¹ Belcher ‘Inside the Black Box’ (n16) 362.

¹¹² Snider, L. (2000) ‘The Sociology of Corporate Crime: An Obituary’, *Theoretical Criminology* 4: 169–206.

reduces the company to no more than a transaction-cost reducing device.

113

Some argue that it is not a theory of the firm to start with, but that it is instead 'a theory of agency costs within a certain type of firm – namely, the corporation'.¹¹⁴ Bodie points out that the theory 'falls apart' as a theory to justify the firm – if a company is truly no more than a nexus of contracts - what then is its purpose in the first place, or by extension the purpose of corporate law.¹¹⁵ Proponents of the theory respond to this by arguing that the contractual nature of the corporation implies terms that the parties have chosen for themselves and these terms, having been freely chosen, are presumably efficient.¹¹⁶ Jensen and Meckling strongly emphasized the fact that companies are private arrangements:

[T]he corporation is *neither* the creature of the state *nor* the object of special privileges extended by the state. The corporation did not draw its first breath of life from either a minister of state or civil servant. More importantly, the corporation requires for its existence only freedom of

¹¹³ Belcher 'Inside the Black Box' (n16) 362.

¹¹⁴ Mathew T. Bodie 'The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm' (2012) 35 *Seattle U. L. Rev.* 1045. The author explains that " Unlike Alchian and Demsetz's firm-which plays a real role in shaping, executing, and enforcing contracts with input providers- the "nexus" at the center of Jensen & Meckling's firm is a mere legal fiction that is "*not an individual*" and has no real independent existence. Jensen and Meckling's model focuses on agency costs created by the upper-level managers who are tasked to do the bidding of principals. Their theory defines agency costs as the costs associated with monitoring by the principal, bonding expenditures by the agent, and the residual loss. The monitoring they describe looks a lot like the "control" that Coase focused on as the key element in defining the firm. But Jensen and Meckling turn their attention to the relationship between shareholders (principals) and management (agents), rather than the relationship of employees to the firm. Their model joins the financial structure of the firm with the management structure of corporate governance. As other commentators have pointed out, the nexus of contract theory is thus not really a theory of the firm at all. Rather, it is a theory of agency costs within a certain type of firm-namely, the corporation.

¹¹⁵ Bodie (n3) 1047.

¹¹⁶ Bodie (n3) 1047.

contract. Corporate vitality in no way is dependent on *special* dispensation from the authorities.¹¹⁷

Hence, contractarianism presents corporate governance as a creature of contract and not of regulation. In other words, the purpose of the state as ‘regulator’ within this paradigm reduced essentially to that of facilitator – its regulatory functions merely to ‘supply the most popular governance ‘terms’ to corporate participants on an ‘off-the-shelf’ basis, so as to save participants (principally shareholders) the extensive transaction costs that would otherwise be involved in devising such norms from scratch. Over and above this base facilitative level of involvement, however, the state is perceived as having no further material role to play in engendering effective managerial accountability within public corporations.’¹¹⁸

But, given the very nature of contractarian theory, how can mandatory rules ever be justified? And mandatory rules in corporate laws are a fact of life. The mere fact that such a large number of these rules are mandatory and apply across the board regardless of preference ‘sits uneasily alongside the dominant contractarian portrayal of corporate laws as being the flexible, instrumental and *non*-socially-determinative outcomes of private selection methods based on rational (shareholder and managerial) choice.’¹¹⁹

As legal scholars, Easterbrook and Fischel were sensitive to the logistical challenges presented by a theory that eschews the law. In response to criticisms they emphasized the autonomy that corporations are afforded

¹¹⁷ Michael C. Jensen & William H. Meckling, “Reflections on the Corporation as a Social Invention” (*Controlling the Giant Corporation: A Symposium*, Center for Research in Government Policy and Business, Graduate School of Management, University of Rochester, 1982) as cited by Vasudev (n5) 928 at note 54.

¹¹⁸ Moore *Governance in the Shadow* (n3) 7

¹¹⁹ Moore *Governance in the Shadow* (n3) 5. He identifies the most problematic feature of mandatory rules as being their universal application. By their very nature, they cannot respond to individual preference or ‘firm-specific’ circumstances that may justify exceptions from the rule.

when managing their own affairs and stressed the ‘open character’ of corporate law.¹²⁰ Arguing that the enabling statutes found in most American states allowed managers and investors to ‘write their own tickets,without substantive scrutiny from a regulator and without effective restraint on the permissible methods of corporate governance’¹²¹ they point out that the courts apply the business judgement doctrine in a hands-off approach to corporate managers, affording the law a relatively inconsequential position. Their answer to the inevitable question – why not just abolish corporate law and allow people to contract as they please – is utilitarian at heart.¹²² In essence, they see corporate law as a set of ‘off-the-rack’ terms, allowing participants in corporate ventures to save the costs of contracting. There are numerous terms which one can imagine most companies would want to adopt, and corporate legislation and existing case law are in the business of supplying these terms free of cost, making it possible for entrepreneurs to focus on more pertinent matters.¹²³

But as Vasudev points out, Easterbrook and Fischel describe their answer as not entirely satisfactory – in a sense admitting the limitations of the contractarian approach. He notes that, although it is true that incorporation has evolved from privilege to right, and that the law is minimally intrusive, it is undeniable that corporate and securities law do in fact exist.¹²⁴

Even the staunchest of contractarian scholar will concede that ‘at the most basic level of civil society the fundamental structural preconditions of a market system are dependent on extra – contractual governmental

¹²⁰ Vasudev (n5) 928.

¹²¹ Easterbrook and Fischel (n28) 1417.

¹²² Vasudev (n5) 929.

¹²³ Vasudev (n5) 929.

¹²⁴ The author points out that ‘[i]ncorporation is made possible only by following the procedures prescribed under the corporate statutes that, together with securities laws, govern corporations during their existence. Economic theory fails to deal with this fact in a satisfactory manner.’ Vasudev (n5) 929.

design'.¹²⁵ Contractarians and neo-liberal theorists will in general also concede that it is a legitimate state function to preserve the macro-economic conditions that support sustained market stability (even if only to the extent of producing monetary instruments and setting a national base rate of interest).¹²⁶ And therein lies the rub:

Against this backdrop, it could be surmised that contractarians ...in seeking at once to admit the necessity of – but also significantly limit the permissible ambit of – regulatory state interventionism in private ordering, are proverbially ‘trying to have their cake and eat it’. That is to say, acknowledging that the purportedly self-regulatory domain of private ordering (both in corporate governance matters and in citizens’ socio-economic affairs more generally) is necessarily dependent on an irreducible minimum of governmentally-mandated institutional infrastructure, opens an awkward regulatory ‘can of worms’ for contractarians that could be said to discredit their argument against state interventionism in other – less structurally fundamental – respects.¹²⁷

4 Recent Developments and Looking to the Future

As mentioned earlier, a number of scholars have been reconsidering the contractarian theory and its impact on corporate law scholarship. Some have also tackled specifically the question of appropriate state intervention and regulatory oversight. A number of theories were developed and although it is not possible to offer a comprehensive overview of them all, the following section will give an overview of the salient arguments that have emerged from the research.

¹²⁵ Moore *Governance in the Shadow* (n3) 234.

¹²⁶ Moore *Governance in the Shadow* (n3) 234.

¹²⁷ Moore *Governance in the Shadow* (n3) 235.

Attenborough approaches the contractarian theory from an empirical vantagepoint and takes aim at the ‘myopic economic vision’ of company law that has dominated literature for decades.¹²⁸ A view of the company as a nexus of explicit and implicit contracts logically implies that ‘company law rule making is essentially a variety of contract law.’¹²⁹ On a positive note, the theory allows for spontaneous governance to arise ‘in a decentralised, emergent fashion even within large communities of participants.’¹³⁰ However, contractarianism goes beyond the private nature of corporate governance arrangements and touches on the many interactions between the law and markets. From this standpoint the theory takes on a politico-economic guise and proponents consider conventional regulatory approaches as ‘a largely external and regressive force to be resisted in the interests of efficient profit making.’¹³¹

Using empirical enquiries, Attenborough comes to conclusions that belie two fundamental assumptions that contractarian theory rests upon. First an assumption that individual rationality and uninhibited agreement produce spontaneous governance, and second neo-classical economic assumptions about de-centralised rule making.¹³² The first assumption, he argues, ignores the role of hierarchy within the notional bargaining activities that the contractarian theory rests upon. In reality, he argues, there is a ‘casual and

¹²⁸ To fully reflect the author’s argument, it bears mention that the article does not take aim at the entirety of contractarian theory but sounds a ‘note of objection’ to two fundamental assumptions made by contractarian theorists. First an assumption that individual rationality and uninhibited agreement produce spontaneous governance, and second neo-classical economic assumptions about de-centralised rule making. See Attenborough (n2) 193.

¹²⁹ Attenborough (n2) 224.

¹³⁰ Attenborough (n2) 193.

¹³¹ Attenborough (n2) 224.

¹³² Attenborough (n2) 193. Attenborough argues finally, that these two dimensions – socio-economic pressures resulting from intragroup hierarchies and the influence of the state in the development and operation of private markets – create conditions that privilege financial capital within the notional company.

correlative relationship ... between socio-economic hierarchy and the development of private orders.’ A tiered governance structure prompts those with power to prefer privately generated rules that will maintain the status quo. Weaker participants co-opted into the structure, interact with others in spite of the terms of the arrangement being unfavourable towards them.¹³³ As far as the second assumption is concerned, he argues cogently that ‘private orders do not necessarily emerge without overall design or operate at the margins of more traditional legal or regulatory structures.’ Instead, he argues, there is frequent interaction between law and markets and ‘non-legal systems typically displace in part, *yet rest upon*, the extant legal regime.’¹³⁴ As such, the formal structures of law and politics generally remain a ‘vital pre-requisite for privately generated rule making, and that state interventionism normally constructs the conditions necessary for private orders in all sorts of cooperative interactions.’¹³⁵ Moore echoes these sentiments, and remarks:

Like any effective institutional feature of a supposed ‘free’ and ‘deregulatory’ market system, the contractual principle in UK corporate law – despite outward appearances – does not arise spontaneously out of thin air but rather is underpinned by a sophisticated and pre-ordained public-regulatory infrastructure....¹³⁶

Galanis also considered whether ‘privately derived governance mechanisms as opposed to mandatory institutions, are sufficient to not only establish but also maintain an efficient corporate governance regime.’¹³⁷ He approaches the inquiry by considering the effect of power asymmetry on the dynamics of corporate governance and, in accordance with Attenborough’s

¹³³ Galanis comes to a similar conclusion. See: Galanis (n1) 329.

¹³⁴ Attenborough (n2) 193.

¹³⁵ Attenborough (n2) 194.

¹³⁶ Moore *Governance in the Shadow* (n3) 208.

¹³⁷ Galanis (n1) 329.

conclusions, he finds that the power dynamics inherent in the bargains between the company and its stakeholders have the propensity over time to cumulatively increase the power of stronger parties, while creating a 'vicious spiral' of loss for weaker parties.¹³⁸ This is not the ideal corporate governance outcome, which according to Galanis, is the product of an equilibrium which balances stakeholder interests against the independent interests of the corporation, so that the capabilities of the latter are able to create organizational rent. In a 'Coasean world', this equilibrium can be achieved by contract alone. However, the power imbalances highlighted above undermine this contractual utopia, with governance tending to exacerbate power imbalances and undermine the sought-after co-operative equilibrium. Galanis concludes that 'contract-derived corporate governance mechanisms alone are inherently unstable and unable to balance and synthesize divergent intra-corporate interests' and that 'to overcome these inherent inefficiencies of contractual corporate governance, legally prescribed power balancing institutions are necessary.'¹³⁹ His views echo Attenborough's findings regarding hierarchy and the balance of power within firms, and a propensity for hierarchy to become entrenched under the terms of private ordering.¹⁴⁰

Deakin also, proposes a change in perspective. He suggests an inverted focus of analysis which asks how the phenomenon of the business firm is viewed by the law. Considered from this angle, corporate law becomes more than merely a response to the agency dilemma, but instead represents a manifestation of solutions to the 'collective action problems' that arise in the context of business enterprises, and which have over time become part

¹³⁸ Galanis (n1) 329.

¹³⁹ Galanis (n1) 330 where the author warns that this is a daunting task: "Stakeholder and company power is drawn from numerous interweaved institutional arrangements in the economy, so that piecemeal regulatory changes or company law alone would be insufficient to resolve power imbalances....[A] systemic approach to corporate governance regulation is needed."

¹⁴⁰ See above at text to note 138.

of the discourse of the legal system. This view sees company law regimes as 'complex emergent phenomena, which have co-evolved alongside the emergence of firms and markets in industrial societies. They have both shaped and been shaped by the long-run processes of economic and technological development associated with industrialization.'¹⁴¹ The aim of corporate law scholarship which is economically informed should be to seek explanations for the many functions that company law performs in a national but also in a global context.¹⁴² Based on principles that emerge from commons research, he posits a model of corporate law which he acknowledges is 'radically at odds with the shareholder-oriented, market focused and globally-driven model of corporate law' that was pervasive from the 1980's until the destruction of the financial crisis. The model he suggests should be based on 'multi-stakeholder governance in preference to shareholder primacy; autonomy for rule-making processes at the level of internal enterprise relations in the face of external capital market pressures; and respect for local and national democratic choices on how to regulate the business firm in the face of pressures to condone or encourage transnational regulatory arbitrage and avoidance.'¹⁴³

As mentioned in chapter 4 above, Deakin argued that the shareholder primacy model which has dominated discourse for near 30 years falls short as it fails to describe core aspects of the legal model of the business enterprise.¹⁴⁴ In summation he argues that the firm should be seen as a 'collectively managed resource or "commons" which is subject to a number of multiple, overlapping and potentially conflicting property-type claims on the part of the different constituencies or stakeholders that provide value to

¹⁴¹ Deakin (n7) 344.

¹⁴² Deakin (n7) 344.

¹⁴³ Deakin (n7) 379.

¹⁴⁴ In this regard he refers specifically to 'the underpinning provided by law for managerial autonomy, the organizational continuity of the firm and the multi-stakeholder nature of firm-level governance.' Deakin (n7) 380.

the firm'.¹⁴⁵ Drawing on the theory of the commons, he then argues that 'the sustainability of the corporation depends on ensuring proportionality of benefits and costs with respect to the inputs made to corporate resources, and on the participation of the different stakeholder groups in the formulation of the rules governing the management and use of those resources. Viewing the corporation as a commons in this sense is the first step toward a better understanding of the role that the corporate form can play in ensuring wider economic and social sustainability'.¹⁴⁶

Moore also considered the impact of contractarian theory on the development of corporate law.¹⁴⁷ The essential arguments were touched on above¹⁴⁸ and relate to contractarian theory's 'organic' or non-interventionist approach to corporate law, as opposed to a more prescriptive approach.¹⁴⁹ Moore proposes a new dynamic – which essentially 'entails accepting a significantly wider ambit of regulatory state involvement in the development of governance norms at the macro level, as a logically necessary precondition to the effective functioning of Anglo-American corporate governance as a whole.'¹⁵⁰

¹⁴⁵ Deakin (n7) 381.

¹⁴⁶ Deakin (n7) 381. While acknowledging the strengths of contractarian theory others have also argued for a "richer, more comprehensive and inclusive theory of corporations." Vasudev (n5) 958. And at 691 where the author calls for a reconsideration of the role of public policy in guiding corporate governance: "Corporations are creatures of and are governed by the law, which represents the public policy on the subject. In the recent past, statutes have granted corporations considerable free space to organize their affairs. If necessary, the free space can be reviewed in light of this experience. The question of how far public policy must concern itself with guiding corporations and their governance must be examined more intensively"

¹⁴⁷ Moore *Governance in the Shadow* (n3).

¹⁴⁸ See inter alia text to note 95 – 57.

¹⁴⁹ Moore *Governance in the Shadow* (n3) 8.

¹⁵⁰ Moore *Governance in the Shadow* (n3) 6.

He proposed a ‘revised contractarian explanation for regulatory state paternalism in corporate governance’.¹⁵¹ To abstract his suggestion to the ‘barebones’, it holds managerial accountability as the principal rationale for mandatory corporate governance laws. The reasoning behind this is based on the author’s contention that ‘the principal and definitive purpose of corporate governance law should be understood as that of engendering an effective and ongoing process of managerial account-giving to shareholders’.¹⁵² This in turn allows the law to legitimate and sustain the reciprocal power imbalances that underlies public companies. He further argues that the formal accountability of managers¹⁵³ becomes increasingly important in light of the fact that information asymmetry often renders ‘micro-level monitoring’ either impossible or cost-ineffective.¹⁵⁴ He argues that, from the point of view of the investor, it becomes more realistic and even cost-effective to determine relative managerial accountability levels if the primary focal point moves from the micro to the macro level. If managerial account giving is systemic, adherence is likely to ensure that firms trade at a significant premium, due to the fact that the system will enhance power-legitimacy with concomitant reputational advantages which should in turn result in lower micro-costs of capital from the company’s standpoint.¹⁵⁵ He considered this resultant ‘macro-accountability’ as a public good, and contends that ‘state regulation should *supplant* – rather than supplement – private ordering with respect to the internal governance dynamics of the corporate equity relation.’¹⁵⁶ The approach purportedly

¹⁵¹ Moore *Governance in the Shadow* (n3) 257.

¹⁵² Moore *Governance in the Shadow* (n3) 257.

¹⁵³ In other words, legal mandates to give reasoned account on an ongoing basis. For further discussion on accountability and the role thereof see also chapter 7.

¹⁵⁴ Moore *Governance in the Shadow* (n3) 265.

¹⁵⁵ Moore *Governance in the Shadow* (n3) 268. This somewhat simplifies the argument, but a more comprehensive overview is impossible given the limitations of the thesis.

¹⁵⁶ Moore *Governance in the Shadow* (n3) 269 – 271, where the author addresses concerns such as the inevitable ‘free-rider’ problems that would arise if, instead of opting into managerial accountability mechanisms firms were, for example, given the option to opt out instead.

solves two dilemma's faced by classic contractarian theory. The laws, though cost ineffective may still be overall wealth-increasing, and any flexibility that is seen to be lost is essentially fictitious considering how the governance codes are often implemented in practice.¹⁵⁷

5 Conclusion

An intangible abstraction, the limited liability company has perplexed the man on the street and scholars alike since its inception. As Salomon's famous dispute illustrates, Joe public could hardly fathom a legal fiction which would see the company as a 'different person altogether' from the subscribers to the memorandum, even more so if 'the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits.'¹⁵⁸ To be fair to Joe public, in his confusion he most certainly found himself in the company of some preeminent lawyers and politicians at the time. As companies grew in number and influence, the ivory towers took note and scholars started to consider the justification for, and functioning of an entity which was by then ubiquitous. This chapter outlined these scholarly pursuits to show how they have informed and shaped the attitudes of those who draft and apply corporate legislation.

In this regard, the pervasive influence of contractarianism and agency cost theory is apparent. If one considers the facilitative, opt-in/opt-out regime embraced by the South African legislature, it appears that the theory also found favour among the drafters of the 2008 Companies Act.¹⁵⁹ Furthermore, although the Act ostensibly speaks to the interests of stakeholders other than shareholders,¹⁶⁰ the cumulative effect of its

¹⁵⁷ For a further explanation of this conclusion see chapter 7.

¹⁵⁸ *Salomon v Salomon* [1897] A.C. 22 Page 51.

¹⁵⁹ See chapter 1 text to note 83 and onwards.

¹⁶⁰ See also the discussion regarding stakeholder theory and the Act, chapter 4.

provisions remains a far cry from a comprehensive stakeholder-oriented approach. In fact, as chapter 4 argues, at most the legislation can be considered to have adopted the UK's enlightened shareholder value propositions and as chapter 7 will contend, stakeholders other than shareholders remain relatively disenfranchised. To be clear, the aim of this research is not to argue for a stakeholder-oriented approach. However, to the extent that shareholder primacy is associated with contractarianism, it is noteworthy that nothing in the Act conclusively distances it from this norm.

The drafters of the 2008 Act did their work before the repercussions of the financial crisis could be appreciated fully and at a time when contractarianism was still the mainstay of corporate discourse. Since then, many scholars have urged regulators to reconsider the appropriate role of the state as supervisor of corporate affairs. As the analysis above has shown, the contractual nexus at the heart of contractarianism does not exist in a vacuum. To consider it in such a manner disregards the concrete effect that hierarchical structures and power imbalances within the corporation have on the formulation of the notional bargains that make up the nexus of contracts. It also denies evidence that endogenous rules rarely materialise in the absence of at least some regulatory structures that act as scaffolding.

Suggestions along the lines that state mandated rules of corporate governance might be an appropriate regulatory solution are usually met with cries of horror and visions of unwarranted costs, inefficiencies and red-tape, not to mention the impossible task of designing a governance regime able to cater to the needs of the many divergent firms that it would seek to regulate. These complexities are undeniable, but they are not insurmountable and nor are they necessarily incompatible with the core tenets of contractarian theory (albeit an expanded version thereof).

The question that this research seeks to answer, is however a slightly different one. The question is not whether it is advisable for the South African legislature to supplement or supplant the existing corporate governance regime by introducing additional, more comprehensive rules in the form of mandatory mechanisms. The question is whether the courts should interpret the legislation and common law that exists in such a manner that it incorporates soft law principles when applying hard law rules. Is it conceivable that such a judicial intervention could be the best of both worlds? Chapter 8 will address these conclusions in greater detail. However, ancillary matters relating to accountability and the enforcement of corporate laws will also have some bearing on the debate and it is to these matters that chapter 7 will turn.

Chapter 7

Accountability and Enforcement

A central part of company law is thus concerned with providing a framework of rules which, on the one hand, constrains the potential abuse by directors of their powers, whilst on the other hand does not so constrain the directors that the efficiency gains from having a strong centralised management are dissipated. This is an age-old problem for company law and one that is constantly re-visited by successive generations of rule-makers, for no one approach can be shown to have struck the balance in an appropriate manner.¹

1 Introduction

Previous chapters of this thesis offered an overview and analysis of a selection of duties that bind company directors. The preceding chapters considered predominantly whether the rules in question should take the form of black letter law or should be used to inform black letter law, and if so, in which way and to what extent. While it is good and well to ponder the existence and contents of rules and norms (both legally prescribed and otherwise), one can hardly do so without considering their enforcement.² It is especially in the context of 'soft law' that the absence of traditional

¹ Davies PL & Worthington S *Gower's Principles of Modern Company Law* (10th edn Sweet & Maxwell 2016) 462.

² In the words of David Sugarman: 'Access to justice depends upon both the existence of legal rights and the ability to enforce them.' David Sugarman, 'Reconceptualising Company Law: Reflections on the Law Commission's Consultation Paper on Shareholder Remedies: Part 2' (1997) 18 *Co Law* 274, 276. And see: Deidre Ahern 'Directors' duties: broadening the focus beyond content to examine the accountability spectrum' (2011) 33 *D.U.L.J* 116.

sanctions may undermine the efficacy of the regime.³ Similar problems plague remedies contained in black letter law, particularly in the context of public listed companies where (at least in jurisdictions such as South Africa and the United Kingdom) the derivative action to enforce directors' duties, is rarely pursued to fruition.⁴

The question that this chapter considers, relates specifically to the enforcement of the existing directors' duties in terms of black letter law. If these duties are robustly enforced, any role for the governance codes in their application would be affected by this fact. On the one hand, if the statutory remedies already constitute a dynamic counterweight to the exercise of directorial power it begs the question whether there is any need for the additional nuance or detail which an importation of the principles contained in the codes would imply. If, on the other hand, the duties are rarely enforced the potential role of the code could be rendered moot as it would be of no avail to tinker with the substantive contents of a duty that is essentially a lame duck.⁵

In addition, the central question of this research also has to do with enforcement, namely the indirect enforcement of the King Code of Corporate Governance. Chapter 1 spoke briefly to the application and enforcement of both King IV and other corporate governance codes, but the

³ Gill North 'Are Corporate Governance Code Disclosure and Engagement Principles Effective Vehicles for Corporate Accountability? The United Kingdom as a Case Study' (2018) 23 *Deakin LR* 177, 177. And see: Andrew Keay 'Assessing accountability of boards under the UK Corporate Governance Code' (2015) 7 *JBL* 570, 571; E. Wymeersch 'The Enforcement of Corporate Governance Codes' (2006) 6 *J. Corp. L. Stud.* 113.

⁴ John Armour et al 'Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States' (2009) 6(4) *Journal of Empirical Legal Studies* 687, 687 where the authors found private lawsuits against directors of public companies alleging breach of duty are nearly non-existent in the United Kingdom. And see: Andrew Keay, 'The Public Enforcement of Directors' Duties: A Normative Inquiry' (2014) 43 *C.L.W.R* 89; Brenda Hannigan, *Company Law* (4th edn, Oxford 2016) para 11-4.

⁵ There are counter arguments that can be raised against both contentions. These will be considered in this chapter.

issue warrants further consideration. Starting with a brief description of ‘accountability’ as a wider concept,⁶ this chapter will give a more in-depth overview of the well-known ‘comply or explain’ approach to corporate governance and the most recent iteration of this approach, adopted by the drafters of King IV in South Africa – ‘apply or explain’.⁷ To the extent that regulation by means of black letter law as opposed to soft law or market regulation has not been considered in chapter six, it will be discussed further in this chapter to highlight some remaining matters. Following this, it will turn to black letter law and consider the enforcement of the statutory and common law duties and any shortfalls in enforcement that might undermine their operation. In doing so, it will also consider the possible impact of the ‘safe harbour’ provisions in the South African legislation that were modelled on the well-known business judgement rule, perhaps most strongly identified with American law and in particular court driven developments in the US state of Delaware.

2 Accountability and Enforcement

a. Accountability as a General Concept and its Relation to Enforcement

Accountability as a prevalent feature of society has today almost unanimously been accepted as a vital element of any governance regime,

⁶ The concept and related issues will be discussed to the extent that they inform the central research question. For a broad and comprehensive overview of accountability in corporate governance see: Andrew Keay *Board Accountability in Corporate Governance* (2015 Routledge).

⁷ The distinction is nuanced. It essentially envisages greater engagement with the principles as the explanation offered should not stop with why compliance was not possible but should set out how the aims of the principle were otherwise established. See King IV 37.

including those pertaining to companies.⁸ In spite of this, it is an ‘elusive concept’⁹ and it tends to be used ‘in a rather glib or simplistic sense without regard for its proper meaning, especially when the term is deployed by corporate lawyers.’¹⁰

Central to most discussions however, is the idea that accountability implies being answerable and providing account of what has been done.¹¹ It involves taking responsibility for actions and across disciplines the weight of literature seems to support the idea that accountability should entail at least potential consequences for the person or body being called to account.¹² Given all of this, ‘[a]ccountability can be seen as one person requiring a justification by another of what has been done, and the latter being subject to reward or punishment (or at least some negative consequences)’.¹³

Although reducing accountability to no more than ‘the punishment that can be exacted on those held accountable by the ones to whom they are accountable’ is perhaps a step too far, there probably must at the very least

⁸ Keay ‘Assessing accountability’ (n3) 556. For an overview of the roots of the concept in general see also: Mark Bovens ‘Analysing and Assessing Accountability: A Conceptual Framework’ (2007) 13(4) *European Law Journal* 447. And see in general: J. Koppell, ‘Pathologies of Accountability: ICANN and the Challenge of “Multiple Accountabilities Disorder”’ (2005) 65(1) *Public Administration Review* 94; Mark Bovens, Thomas Schillemans and Paul T Hart ‘Does Public Accountability Work? An Assessment Tool’ (2008) 86(1) *Public Administration* 225; Amir N. Licht ‘Accountability and Corporate Governance’ (2002).

⁹ Mark Bovens ‘Analysing and Assessing Accountability: A Conceptual Framework’ (2007) 13(4) *European Law Journal* 447, 448. And see: Keay ‘Assessing accountability’ (n3) 557; where the author calls it an ‘notoriously difficult concept to articulate’.

¹⁰ Marc T Moore ‘The (neglected) value of board accountability in corporate governance’ (2015) 9(1) *Law and Financial Markets Review* 10.

¹¹ Keay ‘Assessing accountability’ (n3) 557.

¹² Keay ‘Assessing accountability’ (n3) 557.

¹³ Keay ‘Assessing accountability’ (n3) 557. To the extent that accountability includes ‘giving account’ Keay argues that the latter must ‘explain and justify’ the actions that were taken by the one giving account. He points out that those endowed with power must justify their decisions; that to be accountable implies that one must clarify the reasons for your actions and supply normative grounds to justify them.

be ‘some possibility of consequences’ that might be of a ‘negative flavour’,¹⁴ with several authors actually considering the possibility of sanctions as part and parcel of accountability.¹⁵ It is in particular as far as potential consequences for transgression are concerned that the Corporate Governance Code is ‘highly problematic in contributing to accountability’ and it manifests that ‘where there is any choice of self-regulation over state regulation, the matter of enforcement is the critical element, and the one that produces the most controversy’.¹⁶

The controversy is likely stoked further by the inextricable link between accountability and legitimacy, as failings of the former inevitably erodes the latter. If power is the initial corporate governance problem, accountability is then posited as the solution to this problem and legitimacy hallmarks its successful implementation to resolve the corporate power problem.¹⁷ Before turning to the enforcement of the corporate governance code, the following section will first consider the statutory remedies that were developed to enforce the duties designed to curb and focus directorial power.

b. ‘Soft Law’: Comply or Explain, the Governance Codes and the Market as Enforcer

As discussed in chapter 1, the UK is one of many jurisdictions that has chosen a more discretionary approach to governance by principle, which assumes that accountability is best achieved through a voluntary code coupled with

¹⁴ Keay ‘Assessing accountability’ (n3) 569.

¹⁵ Mark Bovens ‘Analysing and Assessing Accountability: A Conceptual Framework’ (2007) 13(4) *European Law Journal* 447, 451; R. Mulgan, ‘“Accountability”: An Ever Expanding Concept?’ (2000) 78 *Public Administration* 555; K. Strom, ‘Parliamentary Democracy and Delegation’, in K. Strom *et al.* (eds), *Delegation and Accountability in Parliamentary Democracies* (Oxford University Press, 2003) 62.

¹⁶ Keay ‘Assessing accountability’ (n3) 570. And see: Wymeersch (n3) 118.

¹⁷ Moore MT *Corporate Governance in the Shadow of the State* (Hart 2013) 7.

disclosure on a 'comply or explain' basis – and South Africa has followed suit.¹⁸ This stands in stark contrast to American corporate governance, the underpinning of which has become 'mandatory governance determined by regulation and law' with China following a similar orientation.¹⁹

In the UK context, Adrian Cadbury explained that the code relied on market regulation to turn its recommendations into real improvements and believed that 'it will benefit the market standing of companies to comply with the Code ... and shareholders will have a direct interest in ensuring that the companies in which they invest comply'.²⁰ As such, the drafters of the first UK governance code argued that a combination of the self-interest of boards and shareholder action would be sufficient to ensure compliance. This form of endogenous self-regulation has many ostensible advantages. It is cheap as the market effectively pays for its own regulation. It also addresses information asymmetries in that the market is best positioned to identify and address the obstacles generated by its own activities. Importantly, it might avoid the divisive impact of rules being imposed from on high and in turn ensure a greater degree of buy-in on the part of participants, and avoid dangers of 'crowding out' company directors' innate moral compass with a mass of legal rules.²¹ Finally, at least when compared to statute, it is supposedly able to respond more quickly to changes in the

¹⁸ And see: Bob Tricker *Corporate Governance: Principles, Policies and Practices* (3rd edn, Oxford, 2015) 21. And see: Robert C Bird and Stephen Kim Park, 'Organic Corporate Governance' (2018) 59 *B.C.L.Rev.* 21, 35; Adrian Cadbury 'Restoring trust and confidence in the corporate system' (1992) 3(12) *ICCLR* 403, 405

¹⁹ Tricker (n18) 21. See also: Peter Burbidge 'Creating high performance boardrooms and workplaces - European corporate governance in the twenty first century' (2003) 28(5) *European Law Review* 642 for a comparative overview of governance systems in Europe, the US and the UK at the turn of the century – the crux of which remains applicable.

²⁰ Cadbury (n18) 405.

²¹ David Kershaw 'Corporate Law and Self-Regulation (2015) 5 LSE Law, Society and Economy Working Papers page 3, available online <<http://ssrn.com/abstract=3574201>>.

regulatory landscape.²²

However, some thirty years later it appears the rational self-interest that the Cadbury committee relied upon has brought us only so far, and ‘comply or explain’ turned out not to be the silver bullet once thought. The approach usually leaves enforcement to the shareholders. Yet it is unlikely that the shareholders will always be aware (or at least timeously be aware) if the company falsely asserts compliance with the provisions of the Corporate Governance Code – whether such assertion be intentional or otherwise. This all but eliminates any immediate consequences for the directors and in turn results in a ‘serious breakdown of accountability.’²³ Even if the shareholders consider the explanations offered by the board as inadequate and choose not to accept them, they have little power to act on this.²⁴ In commenting on recent changes in the UK corporate governance landscape, Peter Bailey captured what has been widespread opinion:²⁵

Corporate governance, certainly at the quasi-legislative level, is like marmite: company law folk either love it or hate it. This writer has historically been one of the haters. The reason for this is that as an old-fashioned type I believe that if things aren't enacted into law with appropriate sanctions for failure to comply then some corporate executives will simply not comply (or not comply fully).

This is partly due to what must surely be a deep misunderstanding of what the ‘comply or explain’ model requires from company directors. The idea

²² Kershaw (n21) 3. Though the author points out that ‘self-regulatory bodies also typically provide for time-consuming procedures to effect rule changes. This is because public expectations of due process and consultation typically inform non-state as well as state bodies’.

²³ Keay ‘Assessing accountability’ (n3) 570.

²⁴ MacNeil and X. Li, “‘Comply or Explain’: Market Discipline and Non-Compliance with the Combined Code” (2006) 14 *Corp Gov* 486, 489.

²⁵ Peter Bailey ‘It looks like corporate governance is starting to toughen up (at last)’ (2018) 409 *Company Law Newsletter* 1,1.

that directors are given *carte blanche* to do whatever it is they choose and then simply 'explain' their lack of compliance has proven to be tenacious as a nit.

Firms still follow the principles in a blind and unthinking manner, with 'boilerplate' explanations to tick the necessary boxes. For many the Code is seen as a surrogate piece of quasi-legislation which limits the nuanced tailoring to individual firms that was envisaged and instead turn the governance code into 'a source of bureaucratic illegitimacy in itself.'²⁶ Indeed, if the managers and investors perceive the Code as no more than a formalistic and procedural exercise, detached from the real world of business strategy and firm leadership, the value of the Code as an effective mechanism for managerial accountability is called into question.²⁷

Further concerns relate to the market – a device focussed on efficiency – as an appropriate tool to hold directors accountable. In other words, holding directors accountable might not be the most efficient course of action and might not be in the interests of the shareholders at a given time or in a particular context. Although the market ostensibly enforces by assigning a lower share price to a company in instances where its directors fail to comply or offer inadequate explanations for not doing so, this does not always materialise.²⁸ Non-compliance is rarely penalised in the absence of non-performance. In other words, investors apparently 'depend on financial

²⁶ Moore *Governance in the Shadow* (n17) 275. And see: Marc T Moore 'Whispering Sweet Nothings: The Limitations of Informal Conformance in UK Corporate Governance (2009) 9 *J. Corp. L. Stud.* 95. See also: Alvaro Cuervo 'Corporate Governance Mechanisms: a plea for less code of good governance and more market control' (2002) 10(2) *Corporate Governance* 84,84 where the author laments practices in Civil law jurisdictions with similar effects (despite marked contextual differences between 'Anglo-Saxon' and 'continental European' systems of governance.

²⁷ Moore *Governance in the Shadow* (n17) 276.

²⁸ Keay 'Assessing accountability' (n3) 570; Ahern (n2) 118.

performance as a proxy for non-compliance'.²⁹

Dignam explains how the approach favoured by the United Kingdom dynamically informed that embraced by the OECD Advisory Group on Corporate Governance, which set out to formulate minimum standards on corporate governance to be followed by OECD countries.³⁰ He noted that the final OECD principles had almost no impact in the United Kingdom due to their overtly Anglo-Saxon orientation but warned that their impact in other jurisdictions could be 'less benign'.³¹ Dignam argues that the reaction favoured by the Cadbury, Greenbury and Hampel committees (and later adopted by the OECD principles and indirectly subsumed into regulatory regimes in many other jurisdictions) is the result of 'a particularly British form of regulation' which political scientists often refer to as 'negotiated regulation'.³² It was described by Wilkes as 'arm's length regulation'; 'a regulatory style, which is based on accommodation, mutual respect and negotiation' and is rooted in the importance that British public administration has always attached to the autonomy of the firm. Yet again what it harks back to is respect for property and freedom to contract, and the 'legacy of a non-interventionist, minimalist state'.³³

²⁹ Keay 'Assessing accountability' (n3) 570. And see: MacNeil and Li (n21) 492 where the authors refer to the system as one of 'comply or perform', arguing that shareholders will rarely concern themselves with non-compliance or insipid explanations while the company is performing well.

³⁰ Dignam A 'Exporting corporate governance' (n842) 74.

³¹ Dignam A 'Exporting corporate governance' (n842) 76 where the author notes that '[f]irst, on a very basic level the OECD Principles are not suitable for other corporate cultures where for example worker co-determination is at the core of their corporate system or cross ownership exists. Despite the presence of representatives from Germany and Japan on the Advisory Group, no concessions are made to other corporate cultures. In themselves the Principles appear somewhat harmless as they are non-binding and for guidance only. That, however, is not the end of the matter, the adoption of the Principles by the IMF and the World Bank as part of their assessment criteria for lending is less harmless and may begin the imposition of a foreign corporate culture on Asian, African, South American and continental European states'.

³² Dignam A 'Exporting corporate governance' (n842) 73.

³³ S. Wilks, "The Amoral Corporation and British Utility Regulation" (1997) 2 *New Political Economy* 280.

It must be remembered that '[t]he Cadbury, Greenbury and Hampel committees did not spring from the ether fully formed: they are part of this long tradition of negotiated regulation with government'.³⁴ As utopian as this may sound, Dignam lamented that the approach is akin to the inmates not only running the asylum, but that (for some parts of British industry at least) the inmates were designing, building and running the asylum.³⁵

The approach has other perceived shortcomings, such as the fact that the self-regulator may abuse his knowledge and devise rules that are biased in favour of specific interest groups.³⁶

In response to these shortcomings, MacNeil and Li have suggested that the code should be adopted as a set of default rules in company law, subject to an annual application/disapplication resolution at the annual general meeting. They argue that this would counter the current position, where the 'comply or explain' approach has distanced shareholders from compliance decisions and has concomitantly strengthened the role of the board.³⁷

A final approach bears mention, as it embodies what may be considered a compromise between various approaches. To the extent that enforcement is considered a weakness of the 'Cadbury structure', Finch suggested the possibility of a 'compliance agency' to monitor and enforce compliance. She noted that the difference between such an approach and a 'government commission model' would be that in the case of the former an agency would be charged merely with the enforcement of rules produced by industry

³⁴ Dignam A 'Exporting corporate governance' (n842) 74.

³⁵ Dignam A 'Exporting corporate governance' (n842) 74. As the author explains: 'the financial sector, in particular the banks, were used to negotiated regulation with the Bank of England. Indeed, the Bank of England and the DTI have nominees on the Financial Reporting Council which was responsible for the formation of the corporate governance committees. This negotiated form of regulation offered an ideal solution to release the pressures that had built up without losing control of the agenda.'

³⁶ Kershaw (n21) 4; MacNeil and Li (n21) 494.

³⁷ MacNeil and Li (n21) 492. The authors were of the view that this would not diminish the flexibility ordinarily associated with the code.

itself.³⁸ This is similar to the system that operates in Australia at the moment, which has seen the Australian Securities and Investments Commission (ASIC) play a dynamic role in enforcing corporate governance rules.³⁹

The problems that the comply or explain regime presents are not unique to the United Kingdom and certainly plague the South African landscape as well. In fact, the drafters of King IV found themselves so frustrated by 'box ticking' that they chose to revise the 'comply or explain' approach to the 'apply or explain' measure included in King IV.⁴⁰ Certainly some of the advantages of self-regulation will perhaps be even more pivotal in the South African context. The fact that the tax payer does not have to foot the bill, but that the system is instead financed by the market itself is attractive. A system that avoids additional litigation in a country where the courts are under pressure and court dates are a long time coming is not something to disregard lightly. Conversely, as a developing economy under socio-economic pressure and facing the urgencies of income disparity and racial transformation it can hardly be justified that the systems put in place to manage systemic risk and complexity should be reduced to a begrudgingly prepared boilerplate that ticks the box. In this regard, the argument has been made that in transition economies 'the desirable mix of interactive components of the corporate governance framework tends to be in favour of legislation and regulation, rather than self-regulatory and voluntary

³⁸ Vanessa Finch 'Corporate governance and Cadbury: self-regulation and alternatives' (1994) *JBL* 51, 60. And see: Andrew Keay, 'Public Enforcement' (n4) 89.

³⁹ The question of whether the public enforcement of the governance codes is a different thesis altogether. See as an introduction to the position in Australia: Helen Anderson, Michelle Welsh, Ian Ramsay & Peter Gahan 'The evolution of shareholder and creditor protection in Australia: an international comparison' (2012) 61(1) *ICLQ* 171; Demetra Arsalidou 'The liability of non-executive directors for negligent omissions: a new approach under legislation?' (2002) 23(4) *Co Law* 107; Demetra Arsalidou 'An examination into the recent approach of the courts in articulating a standard of care for company chairpersons in Australia' (2005) 26(5) *Co Law* 155; Joanna Bird 'Regulating the Regulators: Accountability of Australian Regulators' (2011) 35 *MULR* 739; John Lowry 'The Irreducible Core of the Duty of Care, Skill and Diligence of Company Directors: "Australian Securities and Investments Commission v Healey"' (2012) 75(2) *MLR* 249.

⁴⁰ See above note 7.

arrangement' - amongst other reasons because of the fact that the market mechanisms of control are 'not yet sufficiently developed to support ... compliance with self-regulatory norms.'⁴¹

It may well be that it will take more than a tinkering with the contents of the duties to ensure accountability and establish a more robust regime, and that down the line an approach such as the one seen in Australia should be debated. However, as chapter 8 below will argue more comprehensively it is certainly a start, and it is one that need not compromise the many benefits traditionally associated with voluntary or market-based regulation. Having considered the latter, the discussion will now turn to the 'black letter' remedies in South Africa's Companies Act, and whether they provide effective mechanisms by means of which directors' duties can be enforced.

c. Enforcement Through the Companies Act

i. An overview of the Applicable Statutory Remedies

Because company directors owe their duties to the company and not to the shareholders directly, the immediate predicament becomes how these duties can then be enforced, and potential damages recovered should the company suffer a loss because of a breach.⁴² It is in this context that the

⁴¹ Nina Cankar 'Transition Economies and Corporate Governance Codes: Can Self-Regulation of Corporate Governance Really Work' (2005) 5 *J. Corp. Law Stud.* 285. Whether this is entirely true in the South African context stands to be debated, but be that as it may, one must not lose sight of the subtleties of regulation in the context of developing economies. An analysis falls outside of the scope of this research, but for an introduction to the issues see for example: Rachael Ntongho 'Self-regulation of corporate governance in Africa: following the bandwagon?' (2009) 20(12) *ICCLR*427; Joseph E.O. Abugu 'Directors' duties and the frontiers of corporate governance' (2011) 22(10) *ICCLR*322; Nicolae Albu & Maria Madalina Girbina 'Compliance with corporate governance codes in emerging economies: How do Romanian listed companies "comply-or-explain"?' (2015) 15(1) *Corporate Governance* 85; Silvia Fazio 'Corporate governance, accountability and emerging economies' (2008) 29(4) *Co Law* 105.

⁴² This is known as the 'proper plaintiff rule' at common law. It entails that where a wrong is done to the company only the latter has standing to take proceedings

derivative action stands central. A such, a more comprehensive overview of its operation and shortcomings will be provided below. Before doing so, mention must be made of other potential avenues that have been included in South Africa's 2008 Companies Act and that may establish causes of action that indirectly enforce directorial duties or otherwise have the potential to call directors to account.

Section 162 of the Act allows a company, a shareholder, a director, company secretary, prescribed officer or a registered trade union that represents employees (or any other employee representative) to apply to court to have a person declared delinquent or under probation.⁴³ The person must have been a director of the company in question within the 24 months immediately preceding the application.⁴⁴ The section determines that a court *must* make an order declaring a person to be a delinquent director under the circumstances listed. These include for example⁴⁵ that while a

against the wrongdoers. It is also often referred to as the rule of *Foss v Harbottle* as it was in this judgement that it was most famously articulated. See: *Foss v Harbottle* (1843) 2 Hare 461; 67 ER 189. For further analysis of the principle see also: *Letseng Diamonds Ltd v JCI Ltd; Trinity Asset Management (Pty) Ltd v Investec Bank Ltd* 2007 (5) SA 564 (W) at 573574); *Trinity Asset Management (Pty) Ltd v Investec Bank Ltd* 2009 (4) SA 89 (SCA); *Mbethe v United Manganese of Kalahari (Pty) Ltd* 2016 (5) SA 414 (GJ) para 60; and *Lewis Group Ltd v Woollam and Others (1)* [2017] 1 All SA 192 (WCC) para 29 on the role of the principle in South African law.

⁴³ Section 162(2). For a general discussion on delinquency and probation orders see: Jean du Plessis and Piet Delpont 'Delinquent directors' and 'directors under probation': a unique South African approach regarding disqualification of company directors' (2017) *SALJ* 274; Cassim R 'Delinquent Directors under the Companies Act 71 of 2008: *Gihwala v Grancy Property Limited* 2016 ZASCA 35' 2016 (19) *PELJ* 128. See also: *Kukama v Lobelo* 2012 JDR 0663 (GSJ); *Lobelo v Kukama* 2013 JDR 1434 (GSJ); *Msimang v Katuliiba* [2013] 1 All SA 580 (GSJ); *Rabinowitz v Van Graan* 2013 5 SA 315 (GSJ); *Grancy Property Limited v Gihwala* 2014 JDR 1292 (WCC); *Gihwala v Grancy Property Limited* 2017 2 SA 337 (SCA); *Lewis Group Limited v Woollam* 2017 2 SA 547 (WCC).

⁴⁴ Section 162(2)(a). The section also makes provision for the Commission or Panel to apply to court to make such declarations (subsection 3) or for any organ of state responsible for the administration of any legislation (subsection 4) given certain requirements are met.

⁴⁵ The list contains several other grounds for delinquency, such as having acted or consented to act as director whilst ineligible or disqualified in terms of the Act. It

director, the person 'grossly abused the position of director',⁴⁶ or 'took personal advantage of information or an opportunity, contrary to [the Act]'.⁴⁷ Further grounds are that the person, whilst a director, intentionally or by gross negligence, inflicted harm upon the company⁴⁸ or acted in a manner that 'amounted to gross negligence, wilful misconduct or breach of trust in relation to the performance of the director's functions within, and duties to the company; or contemplated in [the Act]'.⁴⁹ The circumstances in terms of these subsections have been collectively categorised as 'substantive abuses of office'.⁵⁰

The authors of Henochsberg emphasise that the remedy should not be conflated with either the personal or representative or statutory derivative action (despite the fact that it possibly contains elements of these remedies).⁵¹ They note that this will lead to confusion and undermine the

would not serve the discussion further to include the entire list. Those grounds that were included are the most relevant for purposes of the issues under consideration in this research.

⁴⁶ Section 162(5)(c)(i). See: *Gihwala and Others v Grancy Property Ltd and Others* [2016] 2 All SA 649 (SCA) para 143 where the court emphasises that the section does not imply a 'trivial misdemeanour or an unfortunate fall from grace' but instead denotes gross abuses of the position of director. The latter has been described as 'obvious and egregious conduct' see: *Lewis Group Ltd v Woollam and Others (1)* [2017] 1 All SA 192 (WCC) para 14. Also *Henochsberg on the Companies Act 71 of 2008* (Issue 18 2018) 566 where the authors emphasise that 'Gross abuse of the position of director' relates to the "position as director" and not to the performance of a person in that position or to the duties or functions of the director, as these are dealt with in subs (5) (c) (iv).

⁴⁷ Section 162(5)(c)(ii). The subsection refers specifically to breaches of section 76(2)(a) of the Act which contains the duty not to use information for personal gain or advantage and not to knowingly cause harm to the company or any of its subsidiaries.

⁴⁸ Section 162(5)(c)(iii).

⁴⁹ Section 162(5)(c)(iv)(aa) – (bb).

⁵⁰ *Grancy Property Limited and Another v Gihwala and Others; In re: Grancy Property Limited and Another v Gihwala and Others* (1961/10; 12193/11) [2014] ZAWCHC 97 (26 June 2014) para 156; confirmed in part on appeal in *Gihwala and Others v Grancy Property Ltd and Others* [2016] 2 All SA 649 (SCA)

⁵¹ *Henochsberg on the Companies Act 71 of 2008* (Issue 18 2018) 565. But cf *Gihwala and Others v Grancy Property Ltd and Others* [2016] 2 All SA 649 (SCA) and *Lewis Group Ltd v Woollam and Others (1)* [2017] 1 All SA 192 (WCC).

importance of the remedy which is not aimed at the enforcement of personal rights in the company law sense, and instead is also directed at the indirect protection of the public.⁵²

Although the remedy has the potential to root out the most egregious of offenders, it is too soon to reach any definite conclusion on how enthusiastically it will be received by applicants or how vigorously it will be applied by the courts. However, considering the wording of the section it is highly doubtful whether a disregard for the provisions of the King code could be grounds for a delinquency order – the exception perhaps, might be a systemic and flagrant disregard for the provisions of the code in the case of a listed entity with resultant actions taken by the Johannesburg Stock Exchange resulting in adverse consequences for the company. Delinquency seems to be aimed at the lowest common denominator and therefore, as long as the governance code is perceived as aspirational and a standard of best practice it will likely not play a significant role in this context.

Commonly known as the ‘oppression remedy’, section 163 gives standing to a shareholder or director of a company to apply to court for relief in three instances.⁵³ Most relevant for purposes of this discussion is the third of these, namely that ‘the powers of a director or prescribed officer of the company, or a person related to the company, are being or have been exercised in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant.’⁵⁴ The provision echoes its

⁵² *Henochsberg on the Companies Act 71 of 2008* (Issue 18 2018) 565. But cf *Gihwala and Others v Grancy Property Ltd and Others* [2016] 2 All SA 649 (SCA) and *Lewis Group Ltd v Woollam and Others (1)* [2017] 1 All SA 192 (WCC).

⁵³ Section 163(1)(a) and (b) determine that: “(a) any act or omission of the company, or a related person, has had a result that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant; (b) the business of the company, or a related person, is being or has been carried on or conducted in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant...”

⁵⁴ Section 163(1)(c).

predecessor (section 252 of the South Africa's 1973 Companies Act) and the jurisprudence developed in relation to this previous equivalent remains relevant in determining what constitutes unfair or oppressive conduct.⁵⁵ The modern iteration of the duties leans itself to applications beyond the narrower confines of its predecessor. If acts by directors fall within the ambit of subsection (1)(c), they are now directly actionable by shareholders and, 'such an act that is in breach of fiduciary or other duties, whether in common law or in terms of the Act, could, like illegal acts, be argued to be *prima facie* unfair.'⁵⁶ To date no case law has tested the boundaries of this and the application of this section in such a context is not clear. Certainly, the section gives the courts a wide discretion as far as remedial action is concerned.

Before turning to the derivative action, a final section that bears mention is section 218 which carries the heading 'civil liability'. Subsection two thereof determines that '[a]ny person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention.'⁵⁷ Because the duties are now statutory, a breach of duty would constitute a contravention of the Act and could be grounds for a claim in terms of this section. However, the fact that shareholders are barred from pursuing reflective loss even in terms of section 218 would imply that it would be rare for members to pursue breaches by directors directly by means of this section. More likely, the loss would be suffered by the company and even in terms of section 218 the shareholders could only pursue it by means of the derivative action. It would

⁵⁵ *Henochsberg on the Companies Act 71 of 2008* (Issue 18 2018) 574(2) and see *Grancy Property Limited v Manala* [2013] 3 All SA 111 (SCA) para 22; *Count Gotthard SA Pilati v Witfontein Game Farm (Pty) Ltd and Others* [2013] 2 All SA 190 (GNP) para 17.12; *Peel v Hamon J&C Engineering (Pty) Ltd* [2013] 1 All SA 603 (GSJ) para 43; *Omar v Inhouse Venue Technical Management (Pty) Limited and Others* 2015 (3) SA 146 (WCC) para 4. *De Villiers v Kapela Holdings (Pty) Ltd and Others* (42781/2015) [2016] ZAGPJHC 278 (14 October 2016) para 75.

⁵⁶ *Henochsberg on the Companies Act 71 of 2008* (Issue 18 2018) 574(4).

⁵⁷ In terms of subsection 218(3), the provisions of the section do not affect the right to any remedy that a person may otherwise have.

then be creditors or employees who could make use of this section under limited circumstances. In the case of a creditor it is unlikely to be preferred above section 22 although it might be used as a claim in the alternative.⁵⁸

ii. The Derivative Action

Section 165 of the Act constitutes a codification of what had been a common law remedy – the derivative action.⁵⁹ The section is an interesting hybrid, drawing strongly from Australian law but also taking on board certain traits of the American derivative action.⁶⁰ In short, it gives standing to a shareholder,⁶¹ a director,⁶² or a registered trade union which represents employees of the company,⁶³ to serve a demand on the company ‘to commence or continue legal proceedings, or take related steps, to protect the interests of the company’.⁶⁴ Once the demand has been served the company can respond either by applying to have it set aside on grounds that it is frivolous, vexatious or without merit,⁶⁵ or the company must respond to the demand by appointing an independent and impartial person or

⁵⁸ Section 22 creates a right of recourse in instances where there has been reckless trading by the company’s directors.

⁵⁹ In terms of subsection 165(1) “[a]ny right at common law of a person other than a company to bring or prosecute any legal proceedings on behalf of that company is abolished, and the rights in this section are in substitution for any such abolished right.”

⁶⁰ For an analysis and comparative review of the provision in general see: MF Cassim *The New Derivative Action under the Companies Act* (Juta 2016) 1314; Kathy Idensohn ‘The Fate of *Foss* under the Companies Act 71 of 2008’ (2012) *SA Merc LJ* 355; Helena H Stoop 2012 *SALJ* 527 553.

⁶¹ Section 165(2)(a). The subsection includes in its ambit persons entitled to be registered as shareholders, and those who are shareholders of related companies

⁶² Section 165(2)(b). The subsection also includes prescribed officers and directors and prescribed officers of related companies.

⁶³ Section 165(2)(c).

⁶⁴ Section 165(2). Subsection 165(2)(d) also allows persons who have been granted leave of the court to [serve a demand], which may be granted only if the court is satisfied that it is necessary or expedient to do so to protect a legal right of that other person.”

⁶⁵ Section 165(3). The company has 15 days following receipt of the demand to make such an application.

committee to investigate its allegations and report back to the board.⁶⁶ Upon receipt of this report (and with 60 days after being served with the demand) the company may either initiate or continue legal proceedings or take related steps to protect the interests of the company as contemplated in the demand,⁶⁷ or it may serve notice on the person who made the demand refusing to comply with it.⁶⁸

Following the 'demand phase', the second stage of the process would allow the person who made the demand to apply to court to bring or continue proceedings 'in the name and on behalf of the company'⁶⁹ provided that the latter had failed to respond or failed to respond appropriately to the demand that was served.⁷⁰ The application may also be brought in instances where the person had been served a notice refusing to comply with the demand provided that the court is satisfied that 'the applicant is acting in good faith; the proposed or continuing proceedings involve the trial of a serious question of material consequence to the company; and it is in the best interests of the company that the applicant be granted leave to commence the proposed proceedings or continue the proceedings, as the case may be'.⁷¹

The section further provides for an application to be brought without a

⁶⁶ Section 165(4)(a). The person or committee must report on "(i) any facts or circumstances (aa) that may give rise to a cause of action contemplated in the demand; or (bb) that may relate to any proceedings contemplated in the demand; (ii) the probable costs that would be incurred if the company pursued any such cause of action or continued any such proceedings; and (iii) whether it appears to be in the best interests of the company to pursue any such cause of action or continue any such proceedings".

⁶⁷ Section 165(4)(b)(i).

⁶⁸ Section 165(4)(b)(ii).

⁶⁹ Section 165(5).

⁷⁰ Specifically, that "the company "(i) has failed to take any particular step required by subsection (4); (ii) appointed an investigator or committee who was not independent and impartial; (iii) accepted a report that was inadequate in its preparation, or was irrational or unreasonable in its conclusions or recommendations; (iv) acted in a manner that was inconsistent with the reasonable report of an independent, impartial investigator or committee."

⁷¹ Section 165(5)(b)(i) – (iii).

demand having been served in ‘exceptional circumstances’.⁷²

Subsection 165(7) then creates a rebuttable presumption that granting leave is not in the best interests of the company if the company has decided not to bring or defend proceedings⁷³ and ‘all of the directors who participated in that decision acted in good faith for a proper purpose; did not have a personal financial interest in the decision, and were not related to a person who had a personal financial interest in the decision; informed themselves about the subject matter of the decision to the extent they reasonably believed to be appropriate; and reasonably believed that the decision was in the best interests of the company.’⁷⁴ Finally, should the court grant leave to a person in terms of the section, it must also make an order determining who is responsible for the remuneration and expenses of the appointed person (or committee)⁷⁵ and the court may at any time make any order it considers appropriate about the costs of the person who applied or was granted leave, the company or any other party to the proceedings.⁷⁶

The common law derivative action faced criticism and was deemed ineffectual, which is what prompted statutory intervention.⁷⁷ Although the codified version is a step in the right direction there are still several points of concern and there are no clear signs yet that the new remedy will be more effective than its common law predecessor.⁷⁸

⁷² Section 165(6)(a) – (c).

⁷³ Or the company has decided to discontinue, settle or compromise the proceedings.

⁷⁴ Section 165(7)(a) – (c).

⁷⁵ Section 165(9).

⁷⁶ Section 165(10).

⁷⁷ Cassim F and others *Contemporary Company Law* (2nd edn Juta 2012) 776.

⁷⁸ For a comprehensive discussion of the issues see: MF Cassim *The new derivative action under the Companies Act: guidelines for judicial discretion* (Juta 2016); ‘MF Cassim ‘Costs orders, obstacles and barriers to the derivative action under section 165 of the Companies Act 71 of 2008’ (2014) 26(1) *SA Mercantile Law Journal* 1; MF Cassim ‘Untangling the requirement of good faith in the derivative action in company law’ (2018) 39(2) *Obiter* 363. And see: M Siems ‘Derivative actions as a global phenomenon’ in S Wrzka, S Van Uytsel & M Siems (eds) *Collective Actions:*

Ahern laments the fact that the law's hands-off approach as far as internal company matters are concerned results in a scenario where companies are given 'freedom to choose how they handle directors' breaches of duty'. Through mechanisms such as ratification and release it is possible for a simple majority to decide that taking action is inconvenient or not in the interests of the company.⁷⁹ Numerous constraints, not least access to information and the costs of litigation would deter shareholders from pursuing directors on behalf of the company in the first place, but it is possible that any such actions could be rendered impossible in law as well.

When applying the remedies above and the duties they aim to enforce, the courts have traditionally been reluctant to interfere with internal company matters and especially avoid second guessing business decisions made by the board. The reasoning behind this is familiar territory and was touched upon in previous chapters. The most recent codification of directors duties in South African law formally incorporates this approach into the 2008 Companies Act in the form of a safe-harbour provision or 'business judgement rule'.⁸⁰ As the contents of this provision might have such a

Enhancing access to justice and reconciling multilayer interests? (Cambridge UP 2012) 95.

⁷⁹ Ahern (n2) 119.

⁸⁰ The term 'business judgement rule' is used here in a loose sense. As will be explained below, the South African version is a far cry from the American rule most closely associated with the term. The latter has generated an extensive body of research. See for example: K Chittur 'The Corporate Director's Standard of Care: Past, Present, and Future' (1985) *Delaware Journal of Corporate Law* 505, Anthony Duggan, Jacob S Ziegel, Jassmin Girgis 'REPAP: A Study in Judicial Review of Business Judgements' (2007) 44 *Canadian Business Law Journal* 279; Lyman PQ Johnson 'Corporate Officers and the Business Judgement Rule' (2005) 60 *Bus Law* 439; A Hamermesh and A Gilchrist Sparks 'Corporate Officers and the Business Judgment Rule: A Reply to Professor Johnson' (2005) 60(3) *Bus Law* 865; Charles Hansen 'The Duty of Care, the Business Judgment Rule, and The American Law Institute Corporate Governance Project' (1993) 48(4) *Bus Law* 1355; Joseph IV Hinsey, 'Business Judgment and the American Law Institute's Corporate Governance Project: the Rule the Doctrine and the Reality' (1984) 52 *George Washington Law Review* 609; Bayless Manning 'Business Judgement Rule and the Director's Duty of

notable impact on the mindset with which the courts will approach directors' duties in South African law in future, it must be considered.

3 Deferring to 'Business Judgement': Judicial and Regulatory Restraint

Directors have always been allowed to delegate – this fact speaks to the simple reality that companies are often big and rather complex organisms that rely on large numbers of employees to function. This was recognised as early as 1925 by Romer J in *City Equitable*,⁸¹ and as Davies and Worthington point out, it is based on this principle that directors involved in recent cases where objective tests were used as measure, managed to escape liability.⁸² However, the authors rightly emphasise that suggestions that a director could abdicate all responsibility after having chosen an appropriate delegate and delegated a task to him or her do not accord with recent developments in the law.⁸³

Delegation and the subsequent responsibility to monitor was perhaps the most important issue before the court in *Secretary of State for Trade and Industry v Baker (No 5) ('Re Barings')*.⁸⁴ In considering the duties of the directors following delegation, Park J surmised that:⁸⁵

the exercise of the power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions. No rule of universal application can be formulated as to the duty referred to ... above. The extent of the duty, and the question whether it has been discharged,

Attention: Time for Reality' (1984) 39 *Bus Law* 1477; Andrew Tunc 'The judge and the businessman' (1986) 102 *Law Quarterly Review* 549; E Norman Veasy 'New Insights into Judicial Deference to Directors' Business Decisions: Should we Trust the Courts?' (1984) 39 *Bus Law* 1461.

⁸¹ 1925 Ch 407 at 428-429. See also discussion of the case above.

⁸² Davies and Worthington (n922) 481.

⁸³ Davies and Worthington (n922) 481.

⁸⁴ [1999] a BCLC 433.

⁸⁵ at 489.

must depend on the facts of each particular case, including the director's role in the management of the company.

As mentioned, the legislation does not per se differentiate between executive and non-executive directors, and when Langley J highlighted the salient feature of the duty of care as it pertains to the non-executive in *Equitable Life Assurance Society v Bowley*,⁸⁶ the learned judge noted that, at least in expression, it does not differ from the duty owed by an executive director although in application it 'may and usually will do so'⁸⁷ but that 'it in any event suffices to say that the extent to which a non-executive director may reasonably rely on the executive directors and other professionals to perform their duties is one in which the law can fairly be said to be developing and is plainly 'fact sensitive'. As a point of departure, Langley J was convinced that a company could look to its non-executive directors at the very least for 'independence of judgement and supervision of the executive management.'⁸⁸

What exactly constitutes 'independence' (and indeed what should be determining factors in establishing same) and the extent of the supervision that is required, remain as unclear as ever. What the dictum again confirmed though, was the fact that although a director may delegate tasks, doing so can be no defence where the delegate was not subsequently monitored appropriately. Adding to the complexity of these inquiries is the fact that courts are called upon to adjudicate the boards failure to act, or failure to act appropriately, after the fact. This predicament is traditionally less pertinent in cases of omissions. It is where the board did act, but the action or decision produced a negative outcome, that the weighing up of the directors' 'business judgement' take centre stage.

⁸⁶ [2004] 1 BCLC 180 at paras 35 – 41.

⁸⁷ At para 35.

⁸⁸ At par 41.

Indeed, where one is concerned with judging action as opposed to inaction matters of hindsight, business judgement and the key purpose of the corporate entity as a vehicle for risk taking, take on added significance. As mentioned,⁸⁹ the courts are reluctant to revisit, with the benefit of hindsight, commercial decisions made by boards of directors, provided of course, that these decisions were taken in good faith and that the directors believed that they were in fact in the best interests of the company. The approach has been that '[t]here is no appeal on merits from management decisions to courts of law; nor will courts assume to act as a kind of supervisory board over decisions within the powers of management honestly arrived at.'⁹⁰ In other words there is, in general, no liability for so-called errors of judgement.⁹¹ This approach is certainly not unique to courts in the UK, and perhaps the most famous manifestation thereof is the American Business Judgement Rule, applied robustly in the state of Delaware.⁹²

The wording of the 2008 Companies Act now echoes these sentiments. Section 76(4) states that:

In respect of any particular matter arising in the exercise of the powers or the performance of the functions of director, a particular director of a company—

⁸⁹ See note 55 above.

⁹⁰ *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821, 832. See also: Worthington – 'The Duty to Monitor: A Modern View of the Directors' Duty of Care' in F Patfield (ed) *Perspectives on Company Law: 2* (London, Kluwer Law International, 1997) at 189, 191-192 where the author observes that "the courts are more reluctant to hold directors to account where the claim is that they acted negligently rather than that they failed to act at all because the former requires the courts to evaluate the merits of different business policies."

⁹¹ Joan Loughrey (ed) *Directors' Duties and Shareholder Litigation in the Wake of the Financial Crisis* (Edward Elgar 2013) 34

⁹² It is notable that the UK did not explicitly incorporate such a rule into the 2006 Companies Act. The South African legislature on the other hand apparently did aim to include a statutory business judgement rule (or safe harbour provision) although the exact implications of the newly enacted provision remain unclear. See below for a more detailed discussion on this section of the 2008 Companies Act and the position in the UK with reference to the rule as it developed in the United States.

- (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.

Section 76 of the 2008 Companies Act states explicitly that a director may rely on the performance of persons specifically referred to in the section, or persons ‘to whom the board may reasonably have delegated, formally or informally by course of conduct, the authority or duty to perform one or more of the board’s functions that are delegable under applicable law’.⁹³ The board may also rely on any ‘information, opinions, recommendations, reports or statements, including financial statements and other financial data, prepared or presented by any of these persons.’⁹⁴

⁹³ 76(4)(b)(i)(aa) – (bb).

⁹⁴ 76(4)(b)(ii). The persons specifically referenced of the statute, are employees of the company ‘whom the director reasonably believes to be reliable and competent in the functions performed or the information, opinions, reports or statements provided’. Also included in section 76(5)(b) are legal counsel, accountants, or other professional persons retained by the company, the board or a committee as to matters involving skills or expertise that the director reasonably believes are matters within the person’s professional or expert competence; or as to which the

The provisions offer a framework and give some guidance to directors and to the courts yet much remains open for interpretation and turns on the reasonable belief or discretion of the director concerned. The wording seems to suggest a subjective enquiry when considering whether the belief to rely on a professional or expert's competence and an objective enquiry when considering whether it was reasonable to place confidence in a board committee. Whether this was done intentionally is not clear. Certainly, there seems to be no apparent reason for the discrepancy. The provisions are particularly relevant to the non-executive director, who will often be beholden to management or other functionaries to provide him or her with information and recommendations to act on and review. The position of the non-executive director, and in particular the independent non-executive director, is unique in this regard.

It is not clear what impact the provisions in the 2008 Companies Act will have on the South African legal position. As is the case with the delegation of tasks,⁹⁵ the common law contained what could be called a 'business judgement rule' even before the enactment of the 2008 Act. There is some debate regarding the origins of the rule (which would have been derived from English common law),⁹⁶ but it was certainly accepted that there was at least a 'principle of judicial restraint in deferring to the business judgment of directors'.⁹⁷ As mentioned, the term itself is originally the product of US

person merits confidence. Finally, in terms of section 76(5)(c), a director may validly rely on a committee of the board of which the director is not a member, unless the director has reason to believe that the actions of the committee do not merit confidence.

⁹⁵ See discussion above.

⁹⁶ See J S McLennan 'Duties of care and skill of company directors and their liability for negligence' (1996) 8 S.A Merc. LJ 94 94. where the author cites the words of Lord Greene M.R from *Re Smith and Fawcett Ltd* [1942] Ch. 304 CA as the apparent origin. See on the other hand: P. Redmond 'The reform of directors' duties' (1992) 15 *University of New South Wales Law Journal* 86 113. who argues that the origins of the common law business judgement rule are to be found in the judgement of Lord Hatherley L.C in *Overend & Gurney & Co v Gurney* (1872) LR 5 HL 480.

⁹⁷ Jean J Du Plessis 'Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 1' (2011) 32(11) *Co Law* 347 348. Although some took this to imply a common law business judgement rule, Du

jurisprudence, but in whatever form it is recognised in Australia or South Africa, Du Plessis warned that 'it has not been developed to a state of sophistication sufficient to make it a common law rule of any significance or a rule comparable to the American business judgment rule'.⁹⁸

In other words, equating the American business judgement rule with a South African or English common-law equivalent would be to compare apples with pears: the so-called common law business judgement rule is a poorly developed rule, derived from the courts' reluctance to interfere with internal company decisions. 'The "American business judgement rule" on the other hand, is highly developed with many nuances (even applying in a special way in specific areas like takeovers, 'within the vicinity of insolvency' and in other situations) and with a massive body of case law and academic literature informing it.'⁹⁹

In the United States, the rule generally serves to relieve a director of liability in instances where they have acted (as opposed to instances where they have failed to act). The rule involves a set of procedural steps which, if complied with, will establish a presumption against negligence operating in favour of the director in questions.¹⁰⁰ It must be pointed out, that the complexity inherent in the American business judgment rule is such that

Plessis points out that none of the cases traditionally quoted as authority actually used the term.

⁹⁸ Jean J Du Plessis 'Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 1' (2011) 32(11) *Co Law* 347, 349. At most literature points to some jurisdictions recognising what may be referred to as a 'business judgement doctrine' but it operates to protect decisions themselves and not to create any evidentiary presumptions. See also: S Lombard 'Importation of a Statutory Business Judgment Rule in South African Company Law: Yes or No?' (2005) 68 *Tydskrif vir die Hedendaagse Romeins Hollandse Reg* 614; Michelle Havenga 'The Business Judgment Rule' (2000) *South African Mercantile Law Journal*; D Botha and Richard Jooste 'A critique of the recommendations of the King Report regarding a director's duty of care and skill' (1997) 73 *South African Law Journal* 65.

⁹⁹ Jean J Du Plessis 'Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 1' (2011) 32(11) *Co Law* 347 349. And see note 79 above and sources cited.

¹⁰⁰ Davies and Worthington (n1) 482.

there is still not absolute consensus about whether it is in fact a presumption acting in favour of the directors (as described above), or whether it is a standard of conduct for directors or in the final instance whether it is a principle of judicial review.¹⁰¹ The Supreme Court of Delaware has preferred the view that the rule ‘posits a powerful presumption in favour of actions taken by directors’.¹⁰²

It is not clear which approach the South African courts will follow when interpreting the version of the rule that made its way into the 2008 Act. It is submitted that the marked differences between the South African legal tradition in this context and that of the United states, make it inherently risky to borrow from American jurisprudence when interpreting the provisions of the 2008 Act. This holds true not only for this section of the legislation but for others that were ostensibly transplanted from American law. Luckily it would appear that the South African courts are alive to these risks.¹⁰³ Given the fact that South African common law on directors’ duties has always had English roots, and given the marked similarities between the South African statutory provisions and the Australian version of a codified business judgement rule, it appears likely that the jurisprudence of these two jurisdictions would offer more appropriate guidance.

The rule was considered by the Law Commissions in the UK, but the codification thereof was deemed unnecessary as the Commissions were of the opinion that the courts would be well aware that they are better equipped to adjudicate conflicts of interest than they are to evaluate

¹⁰¹ Jean J Du Plessis ‘Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 1’ (2011) 32(11) *Co Law* 347 349.

¹⁰² *Cede & Co v Technicolor Inc* 634 A. 3d 361 Del, modified 636 A. 2d 956 (Del. 1994).

¹⁰³ See the recent decision of the Supreme Court of Appeals in *African Banking Corporation of Botswana v Kariba Furniture Manufacturers & others* (228/2014) [2015] ZASCA 69 (20 May 2015) where the court was called upon to consider the relevance of US Chapter 11 proceedings when interpreting the Business Rescue provisions that now form part of the South African legislation. For further commentary on the dangers of interpreting the transplants in the 2008 Companies Act see also: H Stoop and A Hutchison (2017) *PELJ*.

business risks and that it is not ideal to substitute (as Worthington and Davies put it) ‘the courts’ hindsight for the directors’ foresight.’¹⁰⁴

The Australian legislature initially showed similar reluctance to make the rule part of its statutory provisions. However, following developments that rendered the standard of care that directors had to comply with wholly objective, calls for a ‘safe harbour’ were eventually headed.¹⁰⁵ Section 180(2) and (3) of the Australian Corporations Act, 2001 states that directors who make ‘business judgements’¹⁰⁶ would be taken to have met the requirements of the directors’ statutory duty of care and skill found in section 180(1) (or its common law equivalents) in respect of that judgement if they:

- (a) make the judgement in good faith and for a proper purpose; and
- (b) do not have a material personal interest in the subject matter of the judgement; and
- (c) inform themselves about the subject matter of the judgement to the extent they reasonably believe to be appropriate; and
- (d) rationally believe that the judgement is in the best interest of the corporation.

There was some uncertainty about the impact of the provision. Did the incumbent director bear the onus to prove that he or she met the criteria set out in the subsection, or would the plaintiff bear the burden to do so?

¹⁰⁴ Davies and Worthington (n1) 482. Indeed the courts needed no statutory reminder of this and, as per Lord Greene M.R, in *Re Smith and Fawcett Ltd* [1942] Ch. 304 CA. ‘[t]hey [the directors] must exercise their discretion bona fide in what they consider – not what a court considers – is in the interests of the company.’

¹⁰⁵ Jean J Du Plessis ‘Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 2’ (2011) 32(12) *Co Law* 377 377.

¹⁰⁶ “Business judgements” are in turned defined by subsection 180(3) as referring to “any decision to take or not take action in respect of a matter relevant to the business operations of the corporation.”

The matter has not been resolved at appellate level, but in *ASIC v Rich*¹⁰⁷ the court concluded that the burden must be carried by the directors and officers.

The similarities between the sections contained in the South African and Australian legislative provisions are at once apparent. There are, however, some marked differences. Most notably, the South African provision is not restricted in its application to the duty of care and skill alone but can also apply to the fiduciary duty to act in the best interests of the company. What the two pieces of legislation do share, is a lack of clarity in several regards. It is not clear whether the South African legislation places the burden of proof on the director or the plaintiff, nor is it clear whether it attempts to create a presumption in favour of the director or a defence. Stevens and De Beer have argued convincingly that the courts could interpret and apply the business judgement rule in such a manner that it could effectively lower the standard of care demanded by the duty of care, skill and diligence to that of gross negligence only, which might erode any use of the duty of care and skill completely.¹⁰⁸

The business judgement rule speaks directly to the accountability debate in that it embodies what can be called an instinctive restraint when regulating directors. On the one hand, as was discussed at the beginning of this chapter, a legitimate regulatory regime has at its heart accountability and as such most would readily concede that there should be some consequences for directors falling short of their task (unprecise as the definition of this task or the standards relating to it may be). On the other hand, various authors have pointed out that it is essentially the most efficient solution to delegate power to the board of directors and that undue regulation and scrutiny could

¹⁰⁷ [2009] NSWSC 1229. The court, per Justice Austin, acknowledged that the language of the legislation was 'profoundly ambiguous' and that the matter would have to be revisited at the appellate level at [7269]-[7270].

¹⁰⁸ Richard Stevens & Philip de Beer 'The duty of care and skill, and reckless trading: Remedies in flux?' (2016) *SA Merc LJ* 250.

negate these efficiency gains.¹⁰⁹ As Kershaw points out, the agency cost problem is actually a result of a corporate form that makes it possible for professional managers to manage assets and wealth on behalf of investors who possess the necessary funds but may lack managerial skills. If we were to delegate this power, but then monitor directors inappropriately when they exercise it, these efficiency gains are lost.¹¹⁰

Inappropriate regulation may also cause directors to shy away from risk taking, which may not serve to maximise corporate wealth.¹¹¹ If we then believe that the law remains 'lenient' towards directors, we must bear in mind that this is not necessarily an inappropriate state of affairs. When considering the impact that voluntary governance codes could and should have on the interpretation of directors' duties, it bears remembering that there would have to be some 'explanation as to why current commercial practice should dictate the content of our legal norms. And current practice might itself offer a rather confused prescription for the law. For ...there might be such a diversity in the role of directors that no single supposedly more rigorous, duty could capture this diversity.'¹¹²

4 Conclusion

Accountability stands central to the question of how companies and the directors that govern their affairs should be regulated. A system of governance can only be legitimate if it demands from those in control an account of their actions and insists that they face any consequences that

¹⁰⁹ D Kershaw *Company Law in Context: Text and Materials* (Oxford 2009) 188; Davies and Worthington S (n1) 462.

¹¹⁰ Kershaw *Company Law in Context* (n108) 188. Compare also Davies and Worthington S (n1) 462.

¹¹¹ Keay A *Directors' Duties* (Jordan 2009) 176 – 177.

¹¹² C A Riley 'The Company Director's Duty of Care and Skill: The Case for an Onerous but Subjective Standard' (1999) 26(5) *MLR* 698.

may arise in the wake of such a rendering. When considering how to interpret and apply directors duties, and whether the governance codes should play any role in the process, the question must be considered against the backdrop of this fact and must speak to the extent to which accountability can and should be affected by the corporate governance codes and in particular whether a novel mode of application of the codes would enhance or undermine accountability.

It stands to reason that the progressive and more textured contents of corporate governance codes in general, and King IV in particular, could add depth to the existing black letter duties and that this in turn might well result in more robust enforcement and enhanced accountability. But one is again confronted with some of the questions encountered in previous chapters of this thesis that relate to the intricate balancing of interests and goals in regulation and corporate governance. On the one hand the firm belief that the courts and regulators should defer to wisdom of corporate boards and the efficiencies of the market 'do what they do best'. On the other hand, the reality that one after another poor performance, corporate collapses and scandals undermine the legitimacy of the regulatory regime. This is perhaps increasingly relevant in an era where companies are no longer just expected to thrive financially – there increasingly seems to be a tacit understanding that their power and influence at least to some extent demands also that they should pro-actively contribute to socio-economic and environmental well-being.

CHAPTER 8

REMARKS IN CONCLUSION

Needs, motives, and initiatives not acknowledged in statutes energize the corporation. As a response to the forces that shape it, the corporation has accumulated responsibilities unrecognized in traditional corporation law ... With the implied consent of its customers, members, and interested public, the corporation sprang loose long ago from traditional economic and legal models. Any attempt to rebottle this corporate genie in its original vessel is a futile exercise, exposing the inadequacy of outmoded economic models. We should not feel hard pressed to devise controls to restrain a spirit ominously unbottled...The exercise of ethical leadership in organizations requires values and skills in intricate combinations that cannot be prescribed by black letter law.¹

In drafting South Africa's newest corporate laws, much was made of modernising company law and enhancing corporate governance, and although the legislature did take some unconventional steps, the legislation that emerged was mostly along the same non-interventionist lines. In fact, its facilitative stance was a dominant selling point.

However, when it came to corporate governance, the sentiment has been that the regulator should know its place. The mystical force that is 'the market' and the companies that are its minions should be left to find their own equilibrium - lest we blunder in and regulate efficiencies into obsolescence.

In considering the origins of the approach, one finds that it is rooted largely in the contractarian outlook that dominates the discourse in the United

¹ Kenneth R. Andrews 'Corporate Governance Eludes the Legal Mind' (1983) 37 *University of Miami Law Review* 213, 215 in response to the outcry that greeted the publication of the American Law Institute's *Principles of Corporate Governance and Structure*.

States and the non-interventionist, arm's length approach followed in the United Kingdom – the latter of which is also the likely source of the 'negotiated regulation' that seeped into much of the commonwealth's corporate governance philosophy. There is no question that the 'founding fathers' of the movement were acting in the good faith conviction that the system they devised was optimal. But when the committees chaired by Cadbury and others did their work, the expectation was certainly not that the fruits of their labour would be relegated to annual box ticking exercises begrudgingly undertaken by board members.

This thesis set out to evaluate the status quo and to reconsider the role of soft law norms in the interpretation and application of the statutory and common law duties that regulate company directors, and specifically non-executive company directors.

The research considered two fundamental duties that company directors undertake – the duty to act with care, skill and diligence and the duty to act in the best interests of the company – the former one stale, and the latter in a state of flux. It has considered the practical implications of an approach that many authors take for granted and that the South African judiciary seems intent on embracing: an interpretation of directors' duties informed by the soft law provisions found in the Corporate Governance Code, (now) King IV. An analysis of the case law shows that the jurisprudence remains immature. References to the principles contained in the Codes tend to be fleeting and obiter or made without any clear indication of how exactly they relate to the black-letter law being applied or what that implies as far as their legal status is concerned. The courts seem ready to allow the traditional duties to take on the nuances contained in the Code but have done so largely without considering the legal basis of such an approach, or the full policy implications that it might have. The following overview will summarise the key findings of the thesis, before ending with some concluding remarks and final suggestions.

As is the case in many jurisdictions, South African corporate governance principles centre around the role of the independent non-executive director. The system is premised in no small part on the idea of the independent non-executive as an internal watchdog or at the very least as an integral part of the system of checks and balances put in place to prevent rent seeking behaviour and excess on the part of management. Some debate exists regarding the proper role of the independent non-executive, and it may well be that it is not realistic to expect of them to do more than just fulfil a monitoring function. Indeed, given the constraints traditionally associated with the position it is not clear how the independent non-executive can be expected to also play a more active role in framing strategy. Certainly though, one must concede that at the very least the independent non-executive should ensure dynamic engagement with the very principles that insist on his seat at the boardroom table. And yet, given the lackadaisical attitude of many professional managers, and the complex relationship which erodes the legitimacy of the independent non-executive to change this fact, one must question whether the system lives up to its potential.

How should regulators respond to this challenge? There are many potential answers to the question. One might be public enforcement of Corporate Governance Codes, as seen in Australia, and another might be black letter law regulation as seen in the United States. A further option is to indirectly give credence to the governance principles when interpreting the statutory and common law duties – and it is this approach that the thesis has considered.

An analysis of the duty of care and skill made it clear that it is not being used to great effect. There are various reasons for this, not least the difficulties associated with the derivative action and other enforcement mechanisms. However, there is little denying that counsel will remain reluctant to advise clients to pursue a cause of action that has traditionally been interpreted

and applied so that only the very crudest of breaches would lead to a result. The codified version of the duty does little to change this state of affairs, and notably the inclusion of the business judgement rule might effectively pull its last remaining tooth.

One of the challenges that has proven very difficult to resolve has been finding concrete parameters to inform the duty. It is impossible to impose a uniform standard, and difficult to determine whether the standard should reflect existing norms or whether it should be more aspirational in what it requires. A starting point would be to at least define expectations and set out what the role requires. It is argued that it is in this regard that the provisions of King IV could play a useful part. The principles offer an objective metric of expectations. It avoids asking more opaque questions such as 'what would a reasonable director in the position of this director have done' as it gives a concrete job description against which to manage conduct. This is not to say that it is impossible to be in breach of the duty of care and skill if one complies with King IV, but considering the comprehensive nature of the Code's provisions it is certainly unlikely - perhaps even to the extent that it might justify a presumption in the director's favour which could inform the application of the new statutory business judgement rule also.

Where the duty to act in the best interests of the company is concerned, a reasoned reference to King IV might be able to push South African companies to embrace the interests of wider stakeholder groups in a responsible manner and underscore the operation and efficacy of the social and ethics committee introduced by the Act.

The approach raises some flags. First, is it legally tenable given the constraints within which the courts interpret and apply statute and the common law. Second, is it desirable from a normative and/or policy standpoint?

The analysis has shown a well-founded reluctance on the part of the courts to interpret statutory provisions in such a manner that the autonomy of the

legislature is undermined. A liberal interpretation South Africa's Supreme Court of Appeal in the case of *Endumeni* might open the door to King IV's introduction as either existing context or, perhaps more feasibly, as part of context which speaks to the genesis of the text (although as the discussion above has shown the latter has especially been treated with circumspection by the courts in the past). In favour of this argument would be the liberal references to the Code in preparatory reports that informed the drafting of the legislation and clear references in the purposes of the Act itself that it aims to ensure good governance.

However, there are convincing arguments to the contrary. The most recent decision of the SCA on the appropriate interpretation and application of the judgement in *Endumeni* indicates that the courts will not interpret the case's references to context liberally and will therefore not allow extrinsic evidence to be led in order to convince the court of the proper meaning of legislative provisions. The warnings that underlie the exclusionary rule that dominated English law extend to the introduction of an extra-textual material drafted, at the end of the day, by an entity not affiliated with government and that may have its own agendas and concerns that may or may not align with national strategy and policy.

As far as the duty of care and skill is concerned, the legislation does state that statutory liability is 'in terms of the common law of delict'. The duty of care in a delictual context has always depended on reasonableness which has always been determined with reference to the legal perceptions of the community as assessed by the Court. As such, the courts could allow the principles of the code into evidence in that it might speak to an assessment of reasonableness. It is submitted that it is essentially on this basis alone that King IV might be introduced in proceedings against a company director.

There are other caveats. The courts develop the common law incrementally and with circumspection. One must bear in mind that the legislature in a recent wholesale review of corporate law chose not to include any direct

reference to the governance code in the act despite ample opportunity to do so. The decision to codify directors' duties was contentious, and when the legislature did proceed, they opted for a high-level codification (as the legislature in the UK did). Neither the statutory duty of care, skill and diligence nor the statutory duty to act in the best interest of the company detract from or add to the existing common law in any meaningful sense. Add to this the presumption that the legislature does not intend to alter the common law more than is necessary, and the fact that the judiciary should not drive sweeping legislative reforms, and it is not entirely clear that more direct references to the Codes will not amount to overstepping the bounds in the absence of legislative intervention.

There are potential evidentiary concerns as well. The Code as such cannot be incorporated into the statute by reference, nor it is submitted could it be taken to inform the common law enquiry into reasonableness or the determination of the best interests of the company simply because it asserts as much in its own text. Instead, it is submitted, evidence would have to be presented to show its prevalence in a particular context or industry is such that it warrants a development of the common law as it pertains to directors duties to include adherence to the principles of the code in the inquiry into care and skill or the determination of whether a director acted in the best interests of the company. What would constitute such evidence is potentially problematic and it is submitted that some legislative intervention is necessary to address this and some of the other issues raised above. The challenge is less pronounced in the case of listed public entities where compliance with listing rules and requisite disclosure requirements in the legislation would be a guide to establishing a generally applicable 'industry standard'. However, as mentioned above, the generic statements often prepared for these purposes are a far cry from showing compliance with the spirit and not just the letter of the Code. In the context of unlisted public companies and larger private companies the matter is far more intricate. Given that 'expert testimony' is neither allowed nor applicable it is difficult

to see how the court can be convinced that the codes are prevalent to the extent that they should start informing legal norms. It is submitted that the courts' hands should be tied absent some form of legislative acknowledgement of the role of the Code.

Setting aside the practical difficulties considered in the thesis and outlined above, there are obvious policy concerns as well. As mentioned above and considered in the research, the prevailing perception has been that the regulator should intervene as little as possible in corporate life, an approach that reflects a contractarian theory of company law. In line with this, self-regulation has long been seen as optimal given the many advantages it brings such as flexibility, buy-in from industry and the fact that it is a cost-effective model. However, many have questioned the efficacy of the regime, especially following the 2007/2008 financial crisis which again highlighted the deficiencies of the system. Many have also argued that the time has come to reconsider a wholesale acceptance of contractarian theory. Concomitant to a re-evaluation of the shareholder primacy model, it is argued that the contractarian model in its original form is no longer able to stand up in the face of modern realities. It *may be* that some greater degree of regulatory interference is not the bogeyman that will destroy capitalism and lay waste to the efficiencies of the market; just as it *may be* that shareholder primacy is not the best way to ensure thriving entities ready to meet the challenges of this decade and beyond.

However, one must admit that such a 'reading in' could undermine certainty and call on the courts to make decisions of a normative nature which they are not necessarily equipped to do. Some have therefore argued that any revisions such as those being suggested will require a systemic and holistic approach, and not a piecemeal application by the courts – and that is if it is required at all: there are still the original objections that it will add to costs and deter qualified candidates from taking up positions as directors.

These are valid concerns, as are those raised in chapter 5 in relation to the interpretation of the legislation and the common law, the legality of the approach and the evidentiary concerns that arise. It is therefore submitted that the most desirable outcome would be for the statute to directly reference the role of the Code. In the context of public listed entities this would be a relatively simple matter, but more nuance would be required for unlisted public entities and larger private entities. A viable solution might be to use the public interest score already in place to determine whether or not financial statements should be audited, what reporting standard should be applied and whether or not a company should have a social and ethics committee in place. As mentioned briefly in the text, the system awards 'points' based on annual turnover, the number of shareholders and employees, and third-party liability. Given this, and the fact that King IV contains industry specific supplements it is entirely conceivable that the legislation could expressly give the courts permission to take account of its provisions in interpreting the duties and offer broad guidelines on how this is to be done making use of the public interest score.

It is submitted that this is the only manner in which the problems identified in the thesis could be overcome. The approach also speaks to a number of other concerns: it will not relinquish the flexibility of the code, and its contents will still be 'industry driven'. Finally, it is not foreseen that this would cause a 'run on the courts' or open the proverbial floodgates. What is a more likely outcome is that discussions about how to treat the Code in boardrooms will likely change as counsel will have grounds to insist on more dynamic compliance. It is submitted that the approach does not imply a 'higher' standard, but in fact denotes a reasonable standard which can be measured against an objective and industry specific metric.

The preceding discussion attempted to summarise a vast and multi-faceted debate. This is the inevitable consequence of considering a question as fundamental as how to regulate the powerhouse that is the modern limited

liability company in a manner that will ensure efficiency without undermining accountability and create wealth without compromising sustainability. Clearly the landscape is brutal. In the time that it has taken to complete this research, the United Kingdom has seen many giants fall. Even companies the size of Carillion or beloved like Thomas Cook were not spared. Marks & Spencer - one of the nation's darlings - has tumbled from the FTSE 100. In South Africa, the collapse of the Steinhoff group of companies has been reverberating for some two years and this is to say nothing of the large-scale corruption being exposed among the ranks of state-owned entities.

At the moment, statutory remedies are rarely used by shareholders to hold managers accountable. Corporate scandals rarely see management face up to the failures of the companies and independent non-executive directors are hardly ever called to task. The fiduciary duties are applied with a fair degree of vim and vigour (especially those that speak to conflict) but the duty of care and skill bobs like a lame duck in the legislative pond and the duty to act in the best interests of the company takes a myopic and archaic approach to what is expected of company directors.

Meanwhile, the voluntary corporate governance code has gained traction but still struggles for boardroom legitimacy. Independent non-executive directors still lack the credibility to ensure that management sees engagement with the code as more than perfunctory box-ticking.

It is possible that the suggested interaction between the Act and King IV would reinvigorate both. In other words, it could revive and give direction to the stale duty of care and skill and nudge the duty to act in the best interests of the company towards a more stakeholder centric middle ground while at the same time giving added legitimacy to King IV.

The approach would avoid the difficulties traditionally associated with legislating these principles. It would allow for a casuistic and more flexible

approach and in each instance the application of the code would be a considered question of fact and context. In the South African context, the Constitution may give further impetus to such an approach. Given the country's socio-economical context and the challenges this brings about, it is perhaps justifiable to reconsider the role of the state as regulator and move in the direction of a more 'synthetic' approach or top down approach to regulating company directors.

BIBLIOGRAPHY

Cases:

South Africa

Abrahamse v East London Municipality and Another; East London Municipality v Abrahamse. 1997 (4) SA 613 (SCA)

African Claim & Land Co Ltd v W J Langermann 1905 TS 494 504

Amod v Multilateral Motor Vehicle Accidents Fund (CC) 27-8-1998 (case CCT 4/98 unreported)

Athol Homeowners Association 2019 (3) SA 398 (SCA)

Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School 2008 (5) SA 1 (SCA)

Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs & Others 2004 (4) SA 490 (CC)

Beukes v Knights Deep Ltd 1917 TPD 683

Bills of Costs (Pty) Ltd v The Registrar, Cape 1979 3 SA 925 (A)

Blower v Noorden 1909 TS 890

Bok v Allen 1884 SAR 137

Booyesen v Jonkheer Boerewynmavery (Pty) Ltd and Another [2017] 1 All SA 862 (WCC)

Casserley v Stubbs 1916 TPD 310

Carmichele v Minister of Safety and Security 2001 (4) SA 938 (CC)

Consolidated Diamond Mines of SWA v Administrator SWA 1958 4 SA 572 (A)

Cool Ideas 1186 CC v Hubbard 2014 (4) SA 474 (CC)

Council for Medical Schemes and Another v Selfmed Medical Scheme and Another [2011] ZASCA 207

CSARS v Daikin Air Conditioning South Africa (Pty) Ltd [2018] ZASCA

Dadoo Ltd and Others v D Krugersdorp Municipal Council 1920 AD

Daniels v Campbell 2004 (5) SA 331 (CC)

Dhanabakium v Subramanian 1943 AD 160

Dinkel v Union Government 1929 AD 150

Du Plessis NO v Phelps 1995 (4) SA 165 (C)

Du Plessis NO v Oosthuizen 1999 (2) SA 191 (O)

Ebrahim v Minister of the Interior 1977 (1) SA 665 (A)

Ellert v Commissioner for Inland Revenue 1957 1 SA 483 (A)

Employees of Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd 6418/2011 8 May 2012 (GNP)

Ernst v Commissioner for Inland Revenue 1954 1 SA 318 (A)

Estate Reid v Goodwin 1920 AD 367

Ex parte Lebowa Development Corporation Ltd 1989 (3) SA 71 (T)

Fisheries Development Corporation of SA Ltd v Jorgensen and Another 1980 (4) SA 156 (W)

Harcourt v Eastman, N.O., 1953 (2) SA 424 (N)

Harris v Law Society of the Cape of Good Hope 1917 CPD 449

Howard v Herrigel [1991] 2 All SA 113 (A)

Hubbard v Cool Ideas 1186 CC 2013 (5) SA 112 (SCA)

In re former Highlands Residents: Sonny v Department of Land Affairs 2000 (2) SA 351 (LCC)

In re Trans-African Insurance Co Ltd (in liquidation) 1958 4 SA 324 (W)

Jaga v Dönges NO and Another; Bhana v Dönges NO and Another 1950 (4) SA 653 (A)

Kaplan v Inc Law Society Tvl 1981 2 SA 762 (T)

Kalahari Resources (pty) Ltd v Arcelormittal SA and others [2012] 3 All SA 555 (GSJ)

Law Society of the Cape of Good Hope v C 1986 1 SA 616 (A)

L D v Technology Corporate Management (Pty) Ltd and Others; S D v L D (40036/16; 35926/16) [2018] ZAGPJHC 69 (23 February 2018)

Lennard's Carrying Co. v. Asiatic Petroleum Co. [1915] A.C. 705

Levenstein v S [2013] 4 All SA 528 (SCA)

Levin v Felt & Tweeds Ltd 1951 (2) SA 402

Manyasha v Minister of Law and Order 1992 (2) SA 179 (SCA)

Marshall Industrials Ltd v Khan 1959 (4) SA 694

Mathiba v Moschke 1920 AD 354

Minister of Environmental Affairs v Recycling and Economic Development Initiative of South Africa NPC, Minister of Environmental Affairs v Kusaga Taka Consulting (Pty) Ltd 2018 (3) SA 604 (WCC)

Minister of Justice v Breytenbach 1942 AD 175

Minister of Safety and Security v Sekhoto 2011 (5) SA 367

Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company (2006) 5 SA 333 (W)

Montelindo Compania Naviera SA v Bank of Lisbon & SA Ltd 1969 2 SA 127 (W)

Msimang NO and another v Katuliiba and others [2013] 1 All SA 580 (GSJ)

Natal Joint Municipal Pension Fund v Endumeni Municipality 2012 (4) SA 593 (SCA)

Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa and Another v Bestvest 153 (Pty) Ltd 2012 (5) SA 497 (WCC)

Ngcobo v Van Rensburg 1999 (2) SA 525 (LCC)

Niagra Ltd v Langerman 1913 WLD 188.

Order Manyasha v Minister of Law and Order 1999 (2) SA 179 (SCA)

Osaka Mercantile Steamship Co Ltd v SAR&H 1938 AD 146

Pearl Assurance v Union Government 1934 AD 560

Protective Mining & Industrial Equipment Systems (Pty) Ltd (formerly Hampo Systems (Pty) Ltd) v Audiolens (Cape) (Pty) Ltd 1987 (2) SA 961 (A)

Public Carriers Association and Others v Toll Road Concessionaries (Pty) Ltd and Others 1990 (1) SA 925 (A) at 943

Rand Bank Bpk v Regering van die RSA 1974 4 SA 764 (T)

R v Detody 1926 AD 198

R v Myburgh 1916 CPD 676

R v Ristow 1926 EDL 168.

R v Tebetha 1959 2 All SA 456 (A)

S v Blaauw 1980 1 SA 536 (C)

- S v Dhlamini* 1988 (2) SA 302 (A)
- S v Khanyapa* 1979 1 SA 824 (A)
- S v Makwanyane and Another* 1995 (3) SA 391 (CC)
- S v Mokoena* 1967 1 SA 440 (A) 445A.
- S v Ncokazi* 1980 3 SA 789 (Tk)
- Santy's Wine & Brandy Co (Natal) Ltd v The District Commandant SA Police* 1945 NPD 115
- Secretary for Customs & Excise v Millman* 1975 3 SA 544 (A)
- Seluka v Suskin & Salkow* 1912 TPD 258
- Serious Economic Offences & Others v Hyundai Motor Distributors (Pty) Ltd & Others: In re Hyundai Motor Distributors (Pty) Ltd & Others v Smit NO & Others* 2001 (1) SA 545 (CC)
- Sibakhulu Construction (Pty) Ltd v Wedgewood Village Golf Country Estate (Pty) Ltd* 2013 (1) SA 191 (WCC)
- Silva v CH Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA)
- Skyway Management Ltd v Telkom SA Bpk* 2001 2 SA 779 (T)
- Smyth v Investec Bank Ltd* 2015 JDR 2278 (GP)
- South African Broadcasting Corporation Ltd and another v Mpofu* [2009] 4 All SA 169 (GSJ)
- South African Fabrics Ltd v Millman, NO, and Another* 1972 (4) SA 592
- Standard Bank Investment Corporation v The Competition Commission and Others* 2000 (2) SA 797 (SCA)
- Stellenbosch Wine Trust Ltd v Oude Meester Group Ltd* 1977 2 SA 221 (C)
- Summit Industrial Corporation v Claimants against the Fund Comprising the Proceeds of the Sale of the MV Jade Transporter* 1987 (2) SA 583 (A)
- Swart v Beagles Run Investments 25 (Pty) Ltd* 2011 (5) SA 422 (GNP)
- The City of Tshwane Metropolitan Municipality v Blair Atholl Homeowners Association* (106/2018) [2018] ZASCA 176
- The Trustees of Orange River Land and Asbestos Company v King* (1892) 6 HCG 260
- Thoroughbred Breeders' Association v Price Waterhouse* [2001] 4 All SA 161 (A)

Transnet Ltd t/a Portnet v Owners of the MV "Stella Tingas" and another 2003 (2) SA 473 (SCA)

Tseleng v Chairman, Unemployment Insurance Board 1995 3 SA 162 (T)

Union Government (Minister of Mines) v Thompson 1919 AD 404

University of Cape Town v Cape Bar Council [1986] 2 ALL SA 619 (A)

University of Stellenbosch Legal Aid Clinic and Others v Minister of Justice and Correctional Services and Others 2016 (6) SA 596 (CC)

United Kingdom, United States & Australia

Borella et al v Borden 145 F 2d 63 (1944)

Brady v Brady [1988] BCLC 20 40 (CA)

Caldwell & Co. Ltd v Caldwell, 53 Sc. L.R. 251

Cohen v Selby [2001] 1 BCLC 176

Daniels v Anderson (1995) 16 ACSR 607 664 CA (NSW)

Darvall v North Sydney Brick & Tile Co Ltd (1989) 15 ACLR 230 CA(NSW).

Dodge v Ford 170 N.W. 668 (Mich. 1919)

Dovey v Cory [1901] AC 477, 488, HL

Duke Group Ltd v Pilmer (1999) 31 ACSR 213 340-341 SC(WA)

Fitzsimmons v R (1997) 23 ACSR 355 358 SC (WA)

Gaiman v National Association for Mental Health [1971] Ch. At 330.

Giblin v Mc Mullen (1868) 2 LR 2 PC 317

Gould v Mt Oxide Mines Ltd (in liq) (1916) 22 CLR 490

Harris v North Devon Railway Co (1855) 20 Beav 52 ER 651

HL Bolton (Engineering) Co Ltd v TJ Graham and Sons Ltd [1956] 3 All ER 624

Hutton v West Cork Railway (1883) 23 Ch. D. at 673

In re City Equitable Fire Insurance Co. 1925 Ch 407

Lagunas Nitrate Co v Lagunas Syndicate [1899] 2 Ch 392

Lim Poh Choo v Camden and Islington Local Health Authority [1980] AC 174

Lindgren v L&P Estates Ltd [1968] Ch. 572 CA

- Northern Counties Securities Ltd. v. Jackson & Steeple Ltd.* [1974] 1 WLR 1133
- Ngurli Ltd v McCann* (1953) 90 CLR 425 438 (HC of A)
- Pepper (Inspector of Taxes) v Hart and Related Appeals* [1993] All ER 42 (HL)
- Percival v Wright* [1902] 2 Ch. 421 Ch D.
- Permanent Building Society v McGee* (1993) 11 ACSR 260 289-290 SC (WA)
- Poole v National Bank of China Ltd.*, 1907 A.C. 229
- Rainy Sky SA and others v Kookmin Bank* [2012] *Lloyds Rep* 34 (SC)
- Re Brazilian Rubber Plantations and Estates Ltd* [1911] 1 Ch. 425
- Re Canadian Land Reclaiming and Colonizing Co* (1880) 14 Ch. D. 660
- Re Cardiff Savings Bank* [1892] 2 Ch. 101
- Re Denham & Co.* (1883) 25 Ch.D. 752
- Re Landhurst Leasing Plc, Secretary of State for Trade and Industry v Ball* [1999] 1 BCLC 286
- Re National Provincial Marine Insurance Co (Gilbert's Case)* (1876) 5 Ch App 559
- Re W&M Roith Ltd* [1967] 1 W.L.R. 432
- Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5.
- Russell Kinsela Pty Ltd v Kinsela* (1983) 8 ACLR 384 403 SC (NSW).
- Salomon v A Salomon & Co Ltd* (1987) AC 22
- Secretary of State for Business, Innovation and Skills v Chohan* [2013] EWHC 680 (CH)
- Turquand v Marshall* (1869) 4 Ch App 376
- Vivendi SA v Richards* [2013] EWHC 3006

Legislation:

South Africa

Companies Act 71 of 2008

United Kingdom

Companies Act 2006

Director Disqualification Act 1986

Insolvency Act 1986

Joint Stock Companies Act 1856

Companies Act 1862

Books:

Barnett ML (ed), *Limits to Stakeholder Influence: Why the Business Case Won't Save the World* (Edward Elgar 2018)

Bennion FAR and others, *Bennion on Statutory Interpretation* (5th ed Wildy 2008)

Bennion FAR and others, *Bennion on Statutory Interpretation* (7th ed LexisNexis 2017)

Berle AA and Means GC *The Modern Corporation and Private Property* (1933 The Macmillan Company).

Cassim F and others, *Contemporary Company Law* (2nd edn Juta 2012)

Cheffins BR, *Company Law: Theory, Structure and Operation* (Clarendon Press 1997)

Cheffins BR, *Corporate Ownership and Control: British Business Transformed* (Oxford University Press 2008)

Clarke T, *International Corporate Governance: A Comparative Approach* (2nd edn Routledge 2017)

Cross R, Bell J and Engle G, *Statutory Interpretation* (Butterworths 1995)

- Davies PL & Worthington S, *Gower's Principles of Modern Company Law* (10th edn Sweet & Maxwell 2016)
- Delpont P & Vorster Q, *Henochsberg on the Companies Act 71 of 2008* (Service Issue 18 LexisNexis 2018)
- Demb A & F Neubauer, *The Corporate Board: Confronting the Paradoxes* (1992 Oxford)
- Devenish, GE *Interpretation of Statutes* (Juta 1992)
- Du Plessis JJ and Others, *Principles of Contemporary Corporate Governance* (3rd edn Cambridge University Press 2015)
- Du Plessis JJ and Others, *Principles of Contemporary Corporate Governance* (4th edn Cambridge University Press 2018)
- Du Plessis LM, *Re-Interpretation of Statutes* (Butterworths 2002)
- Du Plessis LM, *Statute Law and Interpretation in 25(1) LAWSA* (Butterworths 2001)
- Filatotchev I and Wright M (eds), *The Life Cycle of Corporate Governance* (Edward Elgar 2005)
- Fleckner AM and Hopt KJ (eds) *Comparative Corporate Governance: A Functional and International Analysis* (CUP 2013)
- Hannigan B, *Company Law* (4th edn, Oxford 2016)
- Keay A, *Directors' Duties* (Jordan 2009)
- Keay A, *The Enlightened Shareholder Value Principle and Corporate Governance* (Routledge 2013)
- Kershaw D, *Company Law in Context: Text and Materials* (Oxford 2009)
- Kraakman R and others, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn Oxford 2017)

Loughrey J (ed), *Directors' Duties and Shareholder Litigation in the Wake of the Financial Crisis* (Edward Elgar 2013)

Markam JW, *A Financial History of Modern U.S. Corporate Scandals from Enron to Reform* (Routledge 2006)

McQueen R, *A Social History of Company Law: Great Britain and the Australian Colonies 1854 – 1920* (Ashgate 2009)

Moore MT, *Corporate Governance in the Shadow of the State* (Hart 2013)

Mortimore S, (ed) *Company Directors – Duties, Liabilities, and Remedies* (3rd edn Oxford 2017)

Naidoo R, *Corporate Governance: An Essential Guide for South African Companies* (Juta 2002)

Olson K, *Watergate: the presidential scandal that shook America* (University Press of Kansas 2003)

Roe MJ, *Political Determinants of Corporate Governance* (Oxford University Press 2003)

Salsbury S, *No Way to Run a Railroad* (McGraw-Hill 1982)

Schudson M, *Watergate in American memory: how we remember, forget, and reconstruct the past* (BasicBooks 1992)

Adam Smith *An Inquiry into the Nature and Causes of the Wealth of Nations* (Methuen & Co 1776)

Sternberg E, *Just Business: Ethics in Action* (2nd edn Oxford 2000)

Steyn, LC *Die Uitleg van die Wette* (5 ed Juta 1981)

Sullivan R, *Statutory Interpretation* (2edn Irwin Law Inc 2007)

Talbot LE, *Critical Company Law* (Routledge Cavendish 2008)

Taylor J, *Creating Capitalism: Joint Stock Enterprise in British Politics and Culture 1800 – 1870* (The Boydell Press, 2006)

Tricker B, *Corporate Governance: Principles, Policies and Practices* (3rd edn Oxford, 2015)

Williamson OE, *The Economic Institutions of Capitalism* (The Free Press 1985).

Woolman S & Bishop M (eds), *Constitutional Law of South Africa* (2nd edn Juta, 2014) Revision Service 6

Yeats JL and others, *Commentary on the Companies Act of 2008* (Juta 2017)

Chapters in Books:

Cheffins BR 'Corporate Governance Reform: Britain as an Exporter' *Corporate Governance and the Reform of Company Law*, Hume Papers on Public Policy: Volume 8 No. 1 (Edinburgh University Press 2000).

Du Plessis JJ 'Corporate Governance: Some Reflections on the South African Law and the German Two-Tier Board System' in F Patfield F (ed), *Perspectives on Company Law: 2* (Kluwer Law International 1997) 131

Hopt KJ, 'Comparative Company Law' in Mathias Reimann & Reinhard Zimmermann (eds) *The Oxford Handbook of Comparative Law* (Oxford 2006) 1161

Jensen MC and Meckling WH 'Corporate Governance and 'Economic Democracy': An Attack on Freedom' in Huizenga CJ (ed), *Proceedings of Corporate Governance: A Definitive Exploration of the Issues* (UCLA Extension 1983) 1

Mitchell LE, 'The Trouble with Boards', in Kieff FC and Paredes TA (eds), *Perspectives on Corporate Governance* (Cambridge University Press 2010) 17.

Siems M 'Derivative actions as a global phenomenon' in S Wrba, S Van Uytsel & M Siems (eds) *Collective Actions: Enhancing access to justice and reconciling multilayer interests?* (Cambridge University Press 2012) 95.

Worthington S, 'The Duty to Monitor: A Modern View of the Director's Duty of Care' in Patfield F (ed), *Perspectives on Company Law: 2* (Kluwer Law International 1997) 18

Journal Articles:

Abugu JE, 'Directors' duties and the frontiers of corporate governance' (2011) 22(10) *International Company and Commercial Law Review* 322

Aghion P and Holden R 'Incomplete Contracts and the Theory of the Firm: What Have We Learned over the Past 25Years?' (2011) 25(2) *The Journal of Economic Perspectives* 181

Ahern D, 'Directors' duties: broadening the focus beyond content to examine the accountability spectrum' (2011) 33 *Dublin University Law Journal* 116

Albu N & Girbina MM, 'Compliance with corporate governance codes in emerging economies: How do Romanian listed companies "comply-or-explain"?' (2015) 15(1) *Corporate Governance* 85

Alchian A A and Demsetz H 'Production, Information Costs, and Economic Organization' (1972) 62(5) *The American Economic Review* 777.

Anderson H, Welsh M, Ramsay I and Gahan P, 'The evolution of shareholder and creditor protection in Australia: an international comparison' (2012) 61(1) *International & Comparative Law Quarterly* 171

Armour J, Black B, Cheffins B, and Nolan R 'Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States'

Arsalidou D, 'An examination into the recent approach of the courts in articulating a standard of care for company chairpersons in Australia' (2005) 26(5) *Company Lawyer* 155

Arsalidou D, 'The liability of non-executive directors for negligent omissions: a new approach under legislation?' (2002) 23(4) *Company Lawyer* 107

Asher C, Mahoney J and Mahoney J 'Towards a Property Rights Foundation for a Stakeholder Theory of the Firm' (2005) 9(5) *Journal of Management and Governance* 29

Attenborough D, 'Empirical insights into corporate contractarian theory' (2017) 37 (2) *Legal studies* 191

Bagley C and Page K, 'The Devil Made Me Do It: Replacing Corporate Directors' Veil of Secrecy with the Mantle of Stewardship' (1999) 36 *San Diego Law Review* 897.

Bainbridge S M 'Director versus Shareholder Primacy in New Zealand Company Law as Compared to U.S.A. Corporate Law' (March 26, 2014). UCLA School of Law, Law-Econ Research Paper No. 14-05. Available at SSRN: <https://ssrn.com/abstract=2416449>

Bainbridge S M 'The Board of Directors as Nexus of Contracts' (2002) 88 *Iowa Law Review* 1

Bainbridge SM 'Director Primacy: The Means and Ends of Corporate Governance' (2002) 97 *NW. U. L. REV.* 547

Bainbridge SM 'The Case for Limited Shareholder Voting Rights' (2006) 53 *UCLA L. REV.* 601

Baum H 'The Rise of the Independent Director: A Historical and Comparative Perspective' Max Planck Private Law Research Paper No. 16/20

Bebchuk LA & Roe MJ 'A Theory of Path Dependence in Corporate Ownership and Governance' (1999) 52(172) *Stanford Law Review* 127

- Bekink M 'An historical overview of the director's duty of care and skill: from the nineteenth century to the Companies Bill of 2007' (2008) SA *Mercantile Law Journal* 95
- Bekink M, 'An historical overview of the director's duty of care and skill: from the nineteenth century to the Companies Bill of 2007' (2008) *South African Mercantile Law Journal* 95.
- Belcher A 'Inside the Black Box: Corporate Laws and Theories' (2003) 12(3) *Social and Legal Studies* 359
- Belcher A 'The Boundaries of the Firm: The Theories of Coase, Knight and Weitzman' (1997) 17 *Journal of Legal Studies* 22
- Bellamy R 'The Political Form of the Constitution: the Separation of Powers, Rights and Representative Democracy' (1996) *Journal of Political Studies* 436.
- Bilchitz D 'Corporate law and the Constitution: Towards binding human rights responsibilities for corporations' (2008) 125(4) *SALJ* 754
- Bird J, 'Regulating the Regulators: Accountability of Australian Regulators' (2011) 35 *Melbourne University Law Review* 739
- Bird RC and Park SK, 'Organic Corporate Governance' (2018) 59 *Boston College Law Review* 21
- Black B & Kraakman R 'A Self-Enforcing Model of Corporate Law' (1996) 109(8) *Harvard Law Review* 1911
- Blair MM & Stout LA 'A Team Production Theory of Corporate Law' (1999) 85 *Va. L. Rev.* 247
- Bodie MT 'The Post-Revolutionary Period in Corporate Law: Returning to the Theory of the Firm' (2012) 35 *Seattle U. L. Rev.* 1033

Botha D and Jooste R 'A Critique of the Recommendations in the King Report Regarding A Director's Duty of Care and Skill' (1997) 114 *South African Law Journal* 65

Botha MM 'Evaluating the Social and Ethics Committee: Is Labour the Missing Link?' (2016) 79(4) *Tydskrif vir Hedendaagse Romeins-Hollandse Reg* 580;

Bouwman N, 'An appraisal of the modification of the director's duty of care and skill' (2009) *South African Mercantile Law Journal* 509.

Bovens M, Schillemans T and Hart PT, 'Does Public Accountability Work? An Assessment Tool' (2008) 86(1) *Public Administration* 225.

Boyle A J 'Company Law and the Non-Executive Director – The USA and Britain Compared' (1978) 27 *International and Comparative Law Quarterly* 487

Branson DM 'The very uncertain prospect of "global" convergence in corporate governance' (2001) *Cornell International Law Journal* 321

Bratton WW 'Enron and the Dark Side of Shareholder Value' (2002) 76 *Tulane Law Review* 1275

Bratton WW 'Self-Regulation, Normative Choice, and the Structure of Corporate Fiduciary Law' (1993) 61 *Geo. Wash. L. Rev.* 1084

Brudney V 'The Independent Director: Heavenly City or Potemkin Village' (1982) 95 *Harvard Law Review* 597

Buckley A and Van der Nat M, 'Derivatives and the Non-executive Director' (2003) 21(3) *European Management Journal* 389.

Burbidge P, 'Creating high performance boardrooms and workplaces - European corporate governance in the twenty first century' (2003) 28(5) *European Law Review* 642

Burke P 'The Higgs Review' (2003) 24(6) *Company Lawyer* 162.

Cadbury A, 'Restoring trust and confidence in the corporate system' (1992) 3(12) *International Company and Commercial Law Review* 403

Campbell A, 'Stakeholders, the Case in Favour' (1997) 30 *Long Range Planning* 446.

Cankar N, 'Transition Economies and Corporate Governance Codes: Can Self-Regulation of Corporate Governance Really Work' (2005) 5 *Journal of Corporate Law Studies* 285.

Carney W 'The Legacy of the "Market for Corporate Control" and the Origins of the Theory of the Firm' (1999) 50 *Case Western Reserve Law Review* 215

Cheffins BR, 'The History of Corporate Governance' (2012) ECGI Law Working Paper N°.184/2012, 2 <<http://ssrn.com/abstract=1975404>> accessed on 20 August 2017.

Cheffins BR, 'The Rise of Corporate Governance in the UK: When and Why' (2015) 68 *Current Legal Problems* 387

Cheung DTY, 'A discussion on whether there is justification in incorporating a stakeholder theory into UK corporate governance for private companies in unregulated transactions' (2018) 39(10) *Company Lawyer* 315, 316

Chirwa MD 'The long march to binding obligations of transnational corporations in international human rights law' (2006) 22(1) *SAJHR* 76

Chittur K, 'The Corporate Director's Standard of Care: Past, Present, and Future' (1985) *Delaware Journal of Corporate Law* 505

Clark B, 'The director's duty of skill and care: subjective, objective or both?' (1999) 27 *Scots Law Times* 239.

Clarke B, 'Corporate responsibility in light of the separation of ownership and control' (1997) 19 *Dublin University Law Journal* 50

Clarke B, 'Duty of care, skill and diligence – from warm baths to hot water' (2016) 56 *Irish Jurist* 139.

Clarke T 'The Continuing Diversity of Corporate Governance: Theories of Convergence and Variety (2016) 16 *Ephemera Theory and Politics in Organization* 19

Clayton R 'Life after *Pepper v. Hart*' (1996) 1 *Judicial Review* 77.

Coase R H 'The Nature of the Firm' (1937) 4(16) *Economica* 386.

Coffee JC (Jr) 'The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role' (1989) 89 *Colum. L. Rev.* 1618

Copp S 'Corporate governance: change, consistency and evolution: Part 1' (2003) 14(2) *International Company and Commercial Law Review* 65.

Crête R 'The Volkswagen Scandal from the Viewpoint of Corporate Governance' 2016 (7) *European Journal of Risk Regulation* 25

Cuervo A, 'Corporate Governance Mechanisms: a plea for less code of good governance and more market control' (2002) 10(2) *Corporate Governance* 84

Danziger Y & Rachum-Twaig O, 'Re-evaluating the justifications for the existence of an independent duty of care' (2014) 35(9) *Company Lawyer* 265.

Dari-Mattiacci G, Gelderblom O, Jonker J & Perotti EC 'The Emergence of the Corporate Form' (2017) 33(2) *The Journal of Law, Economics, & Organization* 193

Davis D, 'How many positivist legal philosophers can be made to dance on the head of a pin? A reply to Professor Fagan' (2012) 129 *SALJ* 59

Davis D, 'The importance of reading—A rebutter to the jurisprudence of Anton Fagan' (2013) 130 *SALJ* 52.

Davis KB 'Structural Bias, Special Litigation Committees and the Vagaries of Director Independence' (2005) 90 *Iowa Law Review* 1305

De Lange 'The Social and Ethics Committee in Terms of the 2008 Companies Act: Some Observations regarding the Exemptions and the Role of the Companies Tribunal' (2015) 27(3) *South African Mercantile Law Journal* 507

De Sloovere FJ, 'Contextual Interpretation of Statutes' (1936) 5(2) *Fordham Law Review* 219

Deakin S 'The Coming Transformation of Shareholder Value' (2005) 13(1) *Corporate Governance: An International Review* 11

Deakin S 'The Corporation as Commons: Rethinking Property Rights, Governance and

Dignam A, 'Exporting corporate governance: U.K. regulatory systems in a global economy' (2000) 21(3) *Company Lawyer* 70

Du Plessis JJ 'A comparative analysis of directors' duty of care, skill and diligence in South Africa and in Australia' 2010 *Acta Juridica* 263

Du Plessis JJ 'Open sea or safe harbour? American, Australian and South African business judgement rules compared: Part 1' (2011) 32(11) *Company Lawyer* 347

Du Plessis JJ, 'A comparative analysis of directors' duty of care, skill and diligence in South Africa and Australia' (2010) *Acta Juridica* 263.

Duchin R, Matsusaka JG & Ozbas O 'When are outside directors effective?' (2010) 96 *Journal of Financial Economics* 195

Duggan A, Ziegel JS, Girgis J, 'REPAP: A Study in Judicial Review of Business Judgements' (2007) 44 *Canadian Business Law Journal* 279

Easterbrook FH and Fischel DR 'The Corporate Contract' (1984) 89 *Columbia Law Review* 1416.

Eisenberg MA, 'Legal Models of Management Structure in the Modern Corporation' (1975) 63 *California Law Review*

Esen R 'Chartered director qualification: professionalism on UK Boards' (2000) 21(9) *Company Lawyer* 287

Esen R 'Managing and monitoring: the dual role of non-executive directors on U.K and U.S boards' (2000) 11(6) *International Company and Commercial Law Review* 202

Esser I & Delport P 'The South African King IV Report on Corporate Governance: is the crown shiny enough?' (2018) 39(11) *Company Lawyer* 378

Esser I 'Codification of directors' duties' (2004) *Juta's Business Law* 26

Esser I and Delport P 'The protection of stakeholders: The South African social and ethics committee and the United Kingdom's enlightened shareholder value approach: Part 1' (2017) 50(1) *De Jure* 97

Esser I and Delport P 'The protection of stakeholders: The South African social and ethics committee and the United Kingdom's enlightened shareholder value approach: Part 2' (2017) 50(2) *De Jure* 221;

Esser I, & MacNeil I, 'Proposed Revisions to the UK Corporate Governance Code: a step forward in recognising a company's responsibilities towards wider stakeholders?' (2018) 39(8) *Company Lawyer* 254, 255

Esser IM 'Corporate social responsibility: A company law perspective' (2011) 23(3) *SA Merc LJ* 317

Executive Director: Creating Accountability in the Boardroom' (2005) 16 *British Journal of Management* S5, S6.

Fagan A, 'A straw man, three red herrings and a closet rule-worshipper — A rejoinder to Davis JP' (2012) 129 *SALJ* 788

Fagan A, 'The secondary role of the spirit, purport and objects of the Bill of Rights' (2010) 127 *SALJ* 611

Fazio S, 'Corporate governance, accountability and emerging economies' (2008) 29(4) 105.

Finch V 'Company Directors: Who Cares About Skill and Care?' (1999) 55(2) *The Modern Law Review* 179

Finch V 'Corporate governance and Cadbury: self-regulation and alternatives' (1994) *Journal of Business Law* 51 – 61

Fisch J E 'Measuring Efficiency in Corporate Law: The Role of Shareholder Primacy' (2006) 31 *J. CORP. L.* 637

Fisher D 'The enlightened shareholder - leaving stakeholders in the dark: will section 172(1) of the Companies Act 2006 make directors consider the impact of their decisions on third parties?' (2009) 20(1) *International Company and Commercial Law Review* 10.

Fort T L & Noone J J 'Banded Contracts, Mediating Institutions, and Corporate Governance: A Naturalist Analysis of Contractual Theories of the Firm' (1999) 62(3) *Law and Contemporary Problems* 163

Freeman E, Wicks AC, and Parmar B 'Stakeholder Theory and "The Corporate Objective Revisited"' (2004) 15(3) *Organization Science* 364

Galanis M 'Vicious Spirals in Corporate Governance: Mandatory Rules for Systemic (Re)Balancing?' (2011) 31(2) *Oxford Journal of Legal Studies* 327

Gelb H 'Corporate Governance and the Independence Myth' (2006) 6 *Wyoming Law Review* 129

Gerner-Beuerle C and Schuster EP, 'The evolving structure of directors' duties in Europe' (2014) 15(2) *European Business Organization Law Review* 191

Gibson K, 'The Moral Basis for Stakeholder Theory' (2000) 26(3) *Journal of Business Ethics* 245

Girvin SD 'The Antecedents of South African Company Law' (1992) 13(1) *The Journal of Legal History* 63

Gold A S 'Theories of the Firm and Judicial Uncertainty' (2012) 35 *Seattle University Law Review* 1087

Gower LCB 'Some Contrasts Between British and American Corporation Law' (1956) 69 *Harvard Law Review* 1360

Greenfield K, 'Saving the World with Corporate Law' (2008) 57 *Emory Law Journal* 947

Grier N 'Enlightened shareholder value: did directors deliver?' (2014) 2 *Juridical Review* 95

Grossman SJ & Hart OD 'The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration' (1986) 94(4) *Journal of Political Economy* 691

Gwanyanya M 'The South African Companies Act and the realisation of corporate human rights and responsibilities' (2015) 18(1) *PELJ* 3101

Hahn R 'Ronald Harry Coase (1910 – 2013): Nobel-prizewinning economist whose work inspired cap-and-trade' (2013) 502 *Nature* 449.

Hamermesh A and Sparks AG, 'Corporate Officers and the Business Judgment Rule: A Reply to Professor Johnson' (2005) 60(3) *The Business Lawyer* 865

Hannigan B 'Board failures in the financial crisis - tinkering with codes and the need for wider corporate governance reforms: Part 1' (2011) 32(12) *Company Lawyer* 363

- Hansen C, 'The Duty of Care, the Business Judgment Rule, and The American Law Institute Corporate Governance Project' (1993) 48(4) *The Business Lawyer* 1355
- Hansmann H & Kraakman R 'The End of History for Corporate Law' (2001) 89 *Georgetown Law Journal* 439
- Hart O and Moore J 'Incomplete Contracts and Renegotiation' (1988) 56(4) *Econometrica* 755.
- Haswell S and Evans E 'Enron, fair value accounting, and financial crises: a concise history' (2018) 31(1) *Accounting, Auditing & Accountability Journal* 25
- Haynes M 'Rationality, morality and Joel Bakan's *The Corporation*' (2007) 3(1) *International Journal of Business Governance and Management* 1
- Healy Michael P. 'Legislative Intent and Statutory Interpretation in England and the United States: An Assessment of the Impact of *Pepper V. Hart*' (1999) 35 *Stanford Journal of International Law* 231
- Hellinx E, 'Steeplechase in the boardroom: the obstacles for non-executive directors to fulfil their role in public companies' (2017) 38(1) *Company Lawyer* 15
- Hicks A 'Directors' liabilities for management errors' (1994) 110 *Law Quarterly Review* 390.
- Higgs R 'Ronald Coase, Anomalous Superstar of the Economics Profession' (2014) 19(2) *The Independent Review* 309
- Himonga C, Taylor M and Pope A 'Reflections on Judicial Views of Ubuntu' (2013) 16 *Potchefstroom Electronic Law Journal* 171.
- Hinsey J, 'Business Judgment and the American Law Institute's Corporate Governance Project: the Rule the Doctrine and the Reality' (1984) 52 *George Washington Law Review* 609

Holden 'A Nobel Prize for Property Rights Theory'

Holdsworth WS 'English Corporation Law in the 16th and 17th Centuries' (1922) 31(4) *The Yale Law Journal* 382.

Hooghiemstra R & Van Manen J 'The Independence Paradox: (im)possibilities facing non-executive directors in The Netherlands' (2004) 12(3) *Corporate Governance: An International Review* 314.

Idensohn K, 'The meaning of 'prescribed officers' under the Companies Act 71 of 2008' (2012) 129(4) *South African Law Journal* 717 – 735

Idensohn K, 'The Regulation of Shadow Directors' (2010) 22(3) *South African Mercantile Law Journal* 326 – 345

Ireland P, 'Property and contract in contemporary corporate theory' (2003) 23(3) *Legal Studies* 453

Jensen M, 'Value Maximisation, Stakeholder Theory and the Corporate Objective Function' (2001) 14 *Journal of Applied Corporate Finance* 8.

Jensen MC & Meckling WH 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 *J. Financ. Econ.* 30

Johnson LPQ, 'Corporate Officers and the Business Judgement Rule' (2005) 60 *The Business Lawyer* 439

Karmel R, 'Implications of the Stakeholder Model' (1993) 61 *George Washington Law Review* 1156;

Karmel R, 'Is the Independent Director Model Broken?' (2013–14) 37 *Seattle Law Review* 775.

Karmel R, 'Is the Independent Director Model Broken?' (2013–14) 37 *Seattle Law Review* 775.

Katzew J 'Crossing the divide between the business of the corporation and the imperatives of human rights—the impact of section 7 of the Companies Act 71 of 2008' (2011) 128(4) *SALJ* 686

- Kay J, 'Theories of the Firm' (2018) 25(1) *International Journal of the Economics of Business* 11.
- Keay A, 'Assessing accountability of boards under the UK Corporate Governance Code' (2015) 7 *Journal of Business Law* 551
- Keay A, 'Section 172(1) of the Companies Act 2006: An Interpretation and Assessment' (2007) 28(4) *Company Lawyer* 106
- Keay A, 'Stakeholder Theory in Corporate Law: Has It Got What It Takes?' (2010) 9 *Richmond Journal of Global Law & Business* 249
- Kershaw D, 'Corporate Law and Self-Regulation (2015) 5 *LSE Law, Society and Economy Working Papers* available online <<http://ssrn.com/abstract=3574201>>.
- Kershaw D, 'The Path of Corporate Fiduciary Law' (2012) 8 *The New York University Journal of Law and Business* 395
- Kiarie S, 'At crossroads: shareholder value, stakeholder value and enlightened shareholder value: Which road should the United Kingdom take?' (2006) 17(11) *International Company and Commercial Law Review* 329.
- Kiarie S, 'Non-executive directors in UK listed companies: are they effective?' (2007) 18 *International Company and Commercial Law Review* 17
- Kloppers HJ, 'Driving Corporate Social Responsibility (CSR) through the Companies Act: An Overview of the Role of the Social and Ethics Committee' (2013) 16(1) *Potchefstroom Electronic Law Journal* 165
- Koppell, 'Pathologies of Accountability: ICANN and the Challenge of "Multiple Accountabilities Disorder"' (2005) 65(1) *Public Administration Review* 94

- Kress JC, 'Board to Death: How Busy Directors Could Cause the Next Financial Crisis' (2018) 59(3) *Boston College L Rev* 877
- Lauritsen H R 'Democracy and the Separation of Powers: A Rancierean Approach' (2010) 11(1) *Distinktion: Scandinavian Journal of Social Theory* 5
- Leech NE & Mundheim RH 'The Outside Director of the Publicly Held Corporation' (1976) 31(4) *The Business Lawyer* 1799
- Linck JS, Netter JM & Yang T 'The Effects and Unintended Consequences of the Sarbanes-Oxley Act on the Supply and Demand for Directors (2009) 22(8) *The Review of Financial Studies* 3287
- Loughrey J, Keay A & Cerioni L, 'Legal Practitioners, Enlightened Shareholder Value and the Shaping of Corporate Governance' (2008) 8 *Journal of Corporate Law Studies* 79
- Loughrey J, Keay A, & Cerioni L, 'Legal Practitioners, Enlightened Shareholder Value and the Shaping of Corporate Governance' (2008) 8 *Journal of Corporate Law Studies* 79
- Lowry J 'The Duty of Loyalty of Company Directors: Bridging the Accountability Gap through Efficient Disclosure' (2009) 68(3) *The Cambridge Law Journal* 607
- Lowry J, 'The Irreducible Core of the Duty of Care, Skill and Diligence of Company Directors: "Australian Securities and Investments Commission v Healey"' (2012) 75(2) *The Modern Law Review* 249
- Lynch E 'Section 172: a ground-breaking reform of director's duties, or the emperor's new clothes?' (2012) 33(7) *Company Lawyer* 196.
- Manne HG 'Mergers and the Market for Corporate Control' (1965) 73 *J. Pol. Econ.* 110.
- Manning B 'The Shareholders' Appraisal Remedy: An Essay for Frank Coker' 72 *Yale L.J.* 223, 245 n.37 (1962).

Manning B, 'Business Judgement Rule and the Director's Duty of Attention: Time for Reality' (1984) 39 *The Business Lawyer* 1477.

Mans-Kemp N, Viviers S and Collins S, 'Exploring the causes and consequences of director overboardedness in an emerging market' (2018) 15 *International Journal of Disclosure and Governance* 210

Mathiopoulos JA, 'The purpose of for profit corporations in light of modern perceptions and wider corporate responsibilities (Part 1)' (2017) 38(9) *Company Lawyer* 278.

McCalman J & Young A 'Another round of corporate governance reforms in the UK: implications for directors in the financial sector' (2018) 33(8) *Journal of International Banking Law and Regulation* 286

McLennan JS, 'Directors' fiduciary duties and the 2008 Companies Bill' (2009) TSAR 184

McLennan JS, 'Duties of care and skill of company directors and their liability for negligence' (1996) 8 S.A Merc. LJ 94

Michaels JD, 'An Enduring, Evolving Separation of Powers' (2015) 115(3) *Columbia Law Review* 515

Milman, D 'Stakeholders in modern UK company law' (2017) 397 *Company Law Newsletter* 1

Moore MT, 'The (neglected) value of board accountability in corporate Governance' (2015) 9(1) *Law and Financial Markets Review* 10

Moore MT, 'Whispering Sweet Nothings: The Limitations of Informal Conformance in UK Corporate Governance' (2009) 9 *J. Corp. L. Stud.* 95

Mukwiri J 'Myth of Shareholder Primacy in English Law' (2013) *European Business Law Review* 217

Muswaka L 'The corporate responsibility for human rights: A conceptual framework' (2014) 5(3) *MJSS* 219

Nolan RC 'Controlling fiduciary power' (2009) 68(2) *Cambridge Law Journal* 294.

Nolan RC, 'The Legal Control of Directors' Conflicts of Interest in the United Kingdom: Non-Executive Directors Following the Higgs Report' (2005) 6 *Theoretical Inquiries in Law* 413, 414.

North G, 'Are Corporate Governance Code Disclosure and Engagement Principles Effective Vehicles for Corporate Accountability? The United Kingdom as a Case Study' (2018) 23 *Deakin Law Review* 177

Ntongho R, 'Self-regulation of corporate governance in Africa: following the bandwagon? (2009) 20(12) *International Company and Commercial Law Review* 427;

Orts E W 'Shirking and Sharking: A Legal Theory of the Firm' (1998) 16 *YALE L. & POL'Y REV.* 265

Pettet B 'The combined code: a firm place for self-regulation in corporate governance' (1998) 13 *Journal of International Banking Law* 394

Pichet E, 'Enlightened Shareholder Theory: Whose Interests Should Be Served by the Supporters of Corporate Governance?' (2011) 8 *Corporate Ownership & Control* 353; 358.

Pornsit Jiraport Seksak Jumreornvong b , Napatsorn Jiraporn c , Simran Singh a 'How do independent directors view powerful CEO's? Evidence from a quasi-natural experiment' (2016) 16 *Finance Research Letters* 268.

Ratner SR 'Corporations and human rights: A theory for legal responsibility' (2001) 111 *Yale LJ* 443

RE Freeman & R Phillips 'Stakeholder Theory: A Libertarian Defence' (2002) 12 *Business Ethics Quarterly* 331

Redmond P 'The reform of directors' duties' (1992) 15 *University of New South Wales Law Journal* 86

- Riley CA 'The Company Director's Duty of Care and Skill: The Case for an Onerous but Subjective Standard' (1999) 26(5) *The Modern Law Review* 697
- Ringe W 'Beyond "Independent" Directors: A Functional Approach to Board Independence' (2006) 119 (5) *Harvard Law Review* 1553
- Ringe W 'Independent Directors: After the Crisis' (2013) 14 *European Business Organization Law Review (EBOR)* 401 – 424
- Roberts J, McNulty T and Stiles P, 'Beyond Agency Conceptions of the Work of the Non-
- Rodrigues U 'The Fetishization of Independence' (2008) 33 *Journal of Corporation Law* 447
- Roederer CJ 'Post-matrix legal reasoning: Horizontality and the rule of values in the South African law' (2003) 19(1) *SAJHR* 57
- Romano R 'After the Revolution in Corporate Law' (2005) 55 *Journal of Legal Education* 342
- Ruggie JG 'Business and human rights: The evolving international agenda' (2007) 101 *AJIL* 819
- Sales LJ 'Modern Statutory Interpretation' (2017) 38(2) *Statute Law Review* 125
- Sales P 'Pepper v Hart: A Footnote to Professor Vogenauer's Reply to Lord Steyn' (2006) 26(3) *Oxford Journal of Legal Studies* 585
- Sarker R 'Daiwa and Barings: A Blueprint for Disaster' (1996) 17 *Company Lawyer* 86
- Scharff MM 'Understanding WorldCom's accounting fraud: did groupthink play a role?' (2005) 11(3) *Journal of Leadership & Organizational Studies* 109
- Schudson M 'Notes on Scandal and the Watergate Legacy' (2004) 47(9) *American Behavioral Scientist* 1231.

Sheikh S and Rees WM, 'Corporate governance and corporate control: self regulation or statutory codification?' (1992) 3 *International Company and Commercial Law Review* 370 – 376

Shleifer A and Vishny R W, 'The Takeover Wave of the 1980s' (1990) 249 *Science, New Series* 745.

Smit L 'Human rights litigation against companies in South African courts: A response to *Mankayi v AngloGold Ashanti* 2011 (3) SA 237 (CC)' (2011) 27(2) *SAJHR* 354

Solaiman SM, 'The landmark James Hardie case in Australia: a wakeup call for non-executive directors' (2013) 34 *Company Lawyer* 180 - 191

Sternberg E, 'The Stakeholder Concept: A Mistaken Doctrine' (1999) *Foundation for Business Responsibilities, Issue Paper No.4* Available online at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=263144 [Accessed 6 July 2019].

Stevens R, & de Beer P, 'The duty of care and skill, and reckless trading: Remedies in flux?' (2016) *South African Mercantile Law Journal* 250

Stevens R, 'The Legal Nature of the Duty of Care and Skill: Contract or Delict?' (2017) 20 *Potchefstroom Electronic Law Journal* 1

Steyn J, 'Pepper v Hart; a Re-Examination' (2001) 21(1) *Oxford Journal of Legal Studies* 59

Stoop HH, 'Towards Greener Companies – Sustainability and the Social and Ethics Committee' (2013) 24(3) *Stellenbosch Law Review* 562

Stout L, 'Bad and Not-So-Bad Arguments for Shareholder Primacy' (2002) 75 *Southern California Law Review* 1189.

Stratton IGC, 'Non-executive directors: are they superfluous?' (1996) 17(6) *Company Lawyer* 162.

Sugarman D, 'Is company law founded on contract or regulation? The Law Commission's paper on company directors' (1999) 20 *Company Lawyer* 162-183

Sugarman D, 'Reconceptualising Company Law: Reflections on the Law Commission's Consultation Paper on Shareholder Remedies: Part 2' (1997) 18 *Company Lawyer* 274, 276.

Sundaram AK and Inkpen AC, 'The Corporate Objective Revisited' (2004) 15(3) *Organizational Science* 350

Sustainability in the Business Enterprise' (2012) 37 *Queen's L.J.* 339

Sweeney-Baird, M 'The role of the non-executive director in modern corporate governance' (2006) 27(3) *Company Lawyer* 67

Talbot L, 'Trying to save the world with company law? Some problems' (2016) 36(3) *Legal Studies* 513

Tomasic R and Akinbami F, 'Towards a new corporate governance after the global financial crisis' (2011) 22(8) *International Company and Commercial Law Review* 237

Vasudev PM 'Law, Economics, and Beyond: A Case for Retheorizing the Business Corporation' (2010) 55 *McGill Law Journal* 911.

Veasey EN 'Should Corporation Law Inform Aspirations for Good Corporate Governance Practices or Vice Versa?' 2001 (149) *University of Pennsylvania Law Review* 2179.

Vogenauer S 'A Retreat from *Pepper v Hart*? A Reply to Lord Steyn' (2005) 25(4) *Oxford Journal of Legal Studies* 629.

Wallis M 'The Common Law's Cool Ideas for Dealing with Ms Hubbard' (2015) (4) *SALJ* 940

Walters A 'Directors' Duties: the impact of the Company Directors Disqualification Act 1986' (2000) 21(4) *Company Lawyer* 110

- Watson S 'How the Company Became an Entity: A New Understanding of Corporate Law' (2015) 1 *Journal of Business Law* 120
- Watson S and Willekes A, 'Economic loss and directors' negligence' (2001) *Journal of Business Law* 217
- Watson S, 'The significance of the source of the powers of boards of directors in UK company law' (2011) 6 *Journal of Business Law* 597
- Wen S, 'Revisiting the corporate objective through the economic lens – the UK perspective' (2013) 24(8) *International Company and Commercial Law Review* 302
- Wickins RJ and Ong CA, 'Confusion worse confounded: the end of the directing mind theory?' (1997) *Journal of Business Law* 524.
- William Bratton, 'The "Nexus-of Contracts" Corporation: A Critical Appraisal' (1989) 74 *Cornell Law Review* 407
- Williams R, 'Enlightened Shareholder Value in UK Company Law' (2012) 35 *U.N.S.W.L.J.* 360
- Williamson OE, 'The Theory of the Firm as Governance Structure: From Choice to Contract' (2002) 16(3) *Journal of Economic Perspectives* 171
- Wilson CH, 'The Separation of Powers under Democracy and Fascism' (1937) 52(4) *Political Science Quarterly* 481 – 504
- Winter RK, 'State Law, Shareholder Protection, and the Theory of the Corporation' (1977) 6 *J. Leg. Stud.* 251.
- Wymeersch E 'The Enforcement of Corporate Governance Codes' (2006) 6 *Journal of Corporate Law Studies* 113
- Wymeersch E, 'The Enforcement of Corporate Governance Codes' (2006) 6 *J. Corp. L. Stud.* 113
- Yan M, 'Why not stakeholder theory?' (2013) 34(5) *Company Lawyer* 148.

Reports and Policy Documents:

Committee on the Financial Aspects of Corporate Governance *Report on the Financial Aspects of Corporate Governance* (1992)

Company Law Review Steering Group *Modern Company Law for a Competitive Economy: Strategic Framework* (1999)

Company Law Review Steering Group *Modern Company Law for a Competitive Economy: Developing the Framework* (2000)

FRC *The UK Corporate Governance Code* (London 2014)

FRC *The UK Corporate Governance Code* (London 2018)

Higgs D *Review of the role and effectiveness of non-executive directors* (2003)

ICGN *ICGN Global Governance Principles* ICGN (London 2014)

Inoxico. *The Inoxico Director Singularity Index: Research Report* (2013)

Irish Law Commission: *Report on Statutory Interpretation* (

Law Reform Commission of Hong Kong: *Report on Extrinsic Materials as an Aid to Statutory Interpretation* (

OECD *G20/OECD Principles of Corporate Governance* (2015 Paris)

SA DTI *South African Company Law for the 21st Century – Guidelines for Corporate Law Reform* (2004)

The Basle Committee on Banking Supervision *Corporate Governance Principles for Banks* Bank for International Settlements (Basle 2014)

The Law Commission and The Scottish Law Commission *The Interpretation of Statutes* (Law Com No. 21) (Scot. Law Com. No.11)

The South African Law Reform Commission *Discussion Paper 112, 'Statutory Revision: Review of the Interpretation [Act 33 of 1957](#) (Project 25)'* (2006)

Walker D *A review of corporate governance in UK banks and other financial industry entities: Final recommendations* (2009)

ASX Corporate Governance Principles and Recommendations (2014) ASX

China Securities Regulatory Commission (2001) *Corporate Governance for Listed Companies in China* CSRC, State Economic Trade Commission, Beijing

News publications:

Friedman, Milton. 1970. "The Social Responsibility of Business is to Maximise Its Profits." <http://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html>

Company Lawyer 'Chairman appointed to group developing corporate governance principles for large private companies' (2018) 39(5) *Company Lawyer* 158.

C Leadbeater, 'Why it Pays to be Good (Eventually)' (2000) *New Statesman* 26 available online at <https://www.newstatesman.com/node/193387>

BBC 'Carillion collapse to cost taxpayers £ 148 m' (7 June 2018) available online at <https://www.bbc.co.uk/news/business-44383224> accessed on 18/07/2019.

BBC 'Thomas Cook bosses face scrutiny over collapse' (24 September 2019) available online at <https://www.bbc.co.uk/news/business-49805014> accessed on 25/09/2019.

