



# SAICA

## DIRECTORS' DUTIES AND RESPONSIBILITIES

**Madelein Burger – 13 September 2021**

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## What do we want to take away from this session?

- Where do we find the "rules"?
- Who can be directors and part of management?
- Are there special rules that apply to corporate actions?
- How do we deal with loans to directors / officers?
- What are their duties, responsibilities and liabilities?
- Committees – what and how do they operate?
- Where does the "King Code" fit into all of this?
- When are directors "excused"?

FOUR SLIDES THAT WOULD NORMALLY FIT “AT THE BACK”

**26 June 2020 - Judge D Unterhalter: High Court of South Africa, Gauteng Local Division, Johannesburg - Dorethea de Bruyn v Steinhoff International Holdings N.V., Steinhoff International Holdings (Pty) Ltd, Deloitte & Touche and Others**

**The case**

- a shareholder of Steinhoff applied for certification of a class action on behalf of certain classes of shareholders;
- alleged: the directors and auditors were negligent and in some instances grossly negligent in making misstatements which caused the share price to be inflated, the shareholders bought at these prices and when the misstatements were made public the price fell, causing damages.

# THE SHAREHOLDER'S (de Bruyn's) ALLEGATIONS

## Conduct falling short of the required standards -

- SIHL, Steinhoff NV, the directors and the auditors failed to carry out their duties, under common law and statutory law duties of care, by overstating the assets, income and profits in the financial statements and understating liabilities and expenses;
- the directors and companies were required to reflect the true position in the financial statements for the benefit of shareholders and failed to do so;
- the financial statements failed to comply with financial reporting standards and did not fairly represent the state of affairs of the companies and they -
  - were false, falsified, misleading and incomplete;
  - failed to accurately show the information; and
  - failed to reference matters which would permit shareholders to appreciate the financial state of affairs and solvency.

## **3 July 2020 - Supreme Court of Appeal of South Africa, Bloemfontein – HLUMISA INVESTMENT HOLDINGS (RF) LTD and EYOMHLABA INVESTMENT HOLDINGS (RF) LTD v LEONIDAS KIRKINIS AND OTHERS (AFRICAN BANK DIRECTORS AND AUDITORS)**

### **The case**

- shareholders of ABIL alleged directors breached section 76(3) as they failed to exercise their powers in good faith and in the best interest of ABIL and African Bank (subsidiary), resulting in the business being carried on recklessly or with gross negligence in contravention of section 22(1) - companies suffered losses, share price to drop from R28,15 to R0.31 between April 2013 and August 2014;
- principle question: whether section 218(2) enables a claim by a shareholder.



# THE ALLEGED MISCONDUCT

## **Directors' alleged breaches of statutory duties**

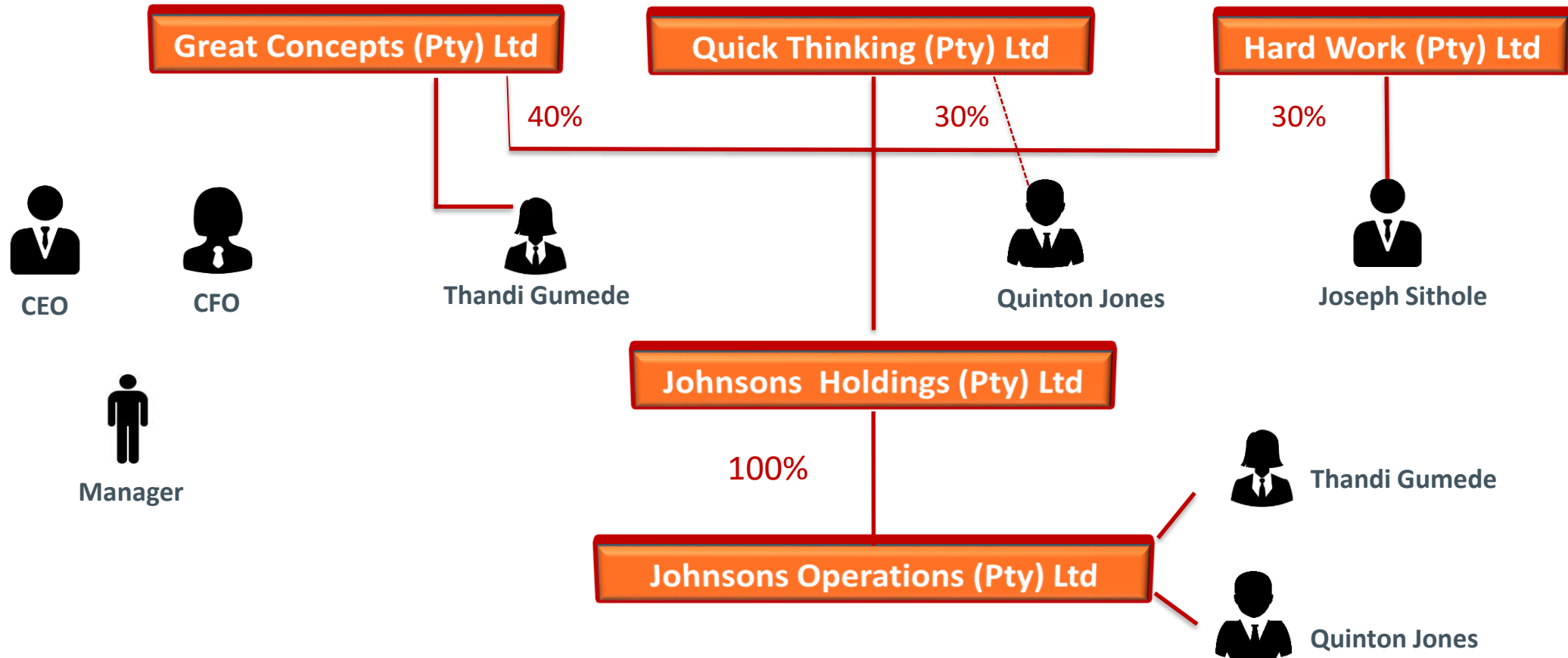
- publication of false financial statements;
- authorisation of a prospectus for a rights issue containing false financial information;
- other information in prospectus misleading;
- authorisation of a loan on contravention of section 45 where foreseeable loan not repayable;
- appointment of an executive director without the necessary skills and expertise;
- failure to provide for losses as a result of bad business decisions;
- using flawed credit provisioning models;
- pursuing aggressive and reckless accounting practices;
- pursuing a rights offer on false premises.

## RELEVANT LEGISLATION AND REGULATIONS

- Companies Act, 2008 ("2008 Act");
- King Report on Corporate Governance ("King IV");
- "Other", e.g. Insurance Act, Financial Sector Regulation Act, 2017.



# BOARD COMPOSITION AND APPOINTMENT



## DIRECTORS AND PRESCRIBED OFFICERS

### **Not automatic - person only becomes director after (section 66(7))**

- appointment / election to the 2008 Act; AND
- delivery of written consent to serve as director.

### **Once appointed by the company**

- irrespective of the CIPC records.

# DIRECTORS AND PRESCRIBED OFFICERS

## **Automatic – a person is a prescribed officer if the person**

- exercises general executive control over and management of the whole, or a significant portion, of the business and activities of the company; or
  - 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,
- irrespective of title or function.

## **Not recorded with CIPC**

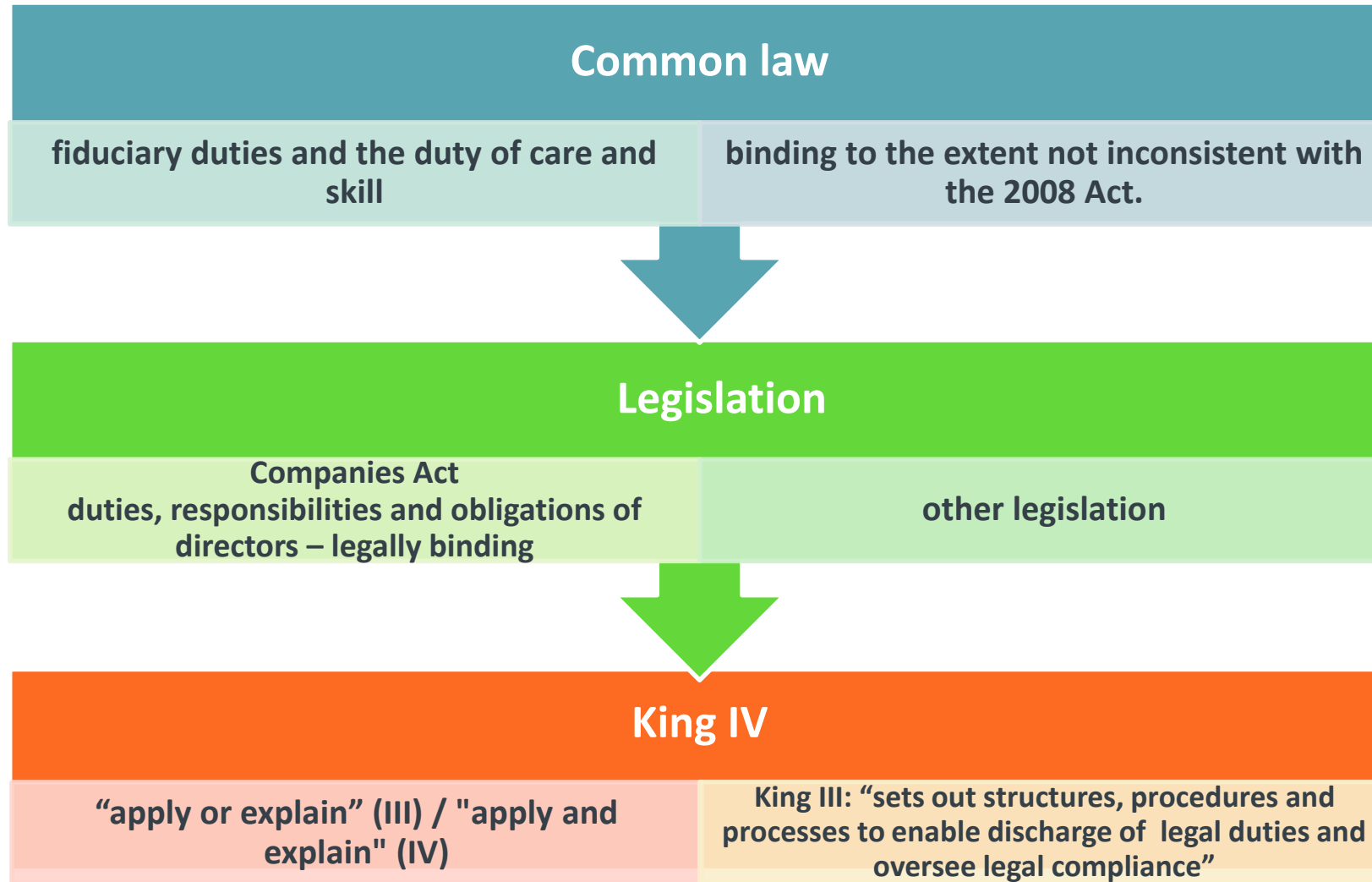
**Issues regarding lenders, observers etc.**

# DIRECTORS AND PRESCRIBED OFFICERS

## **How is a person removed from his office – section 71?**

- directors;
- executive directors who are also employees – remember the Labour Relations Act, 1994;
- prescribed officers.

# DUTIES: THE COMMON LAW, THE 2008 ACT, KING IV



# DUTIES

- **Fiduciary duties in 2008 Act**
  - duty to act in best interest of the company;
  - duty to act in good faith and for a proper purpose;
  - duty regarding information.
- **Other duties under the 2008 Act (to mention a few)**
  - duty to comply with the MOI and rules; duty to provide access to information;
  - process under section 75 if a conflict; accurate information.

# DUTIES

- **Apply to**





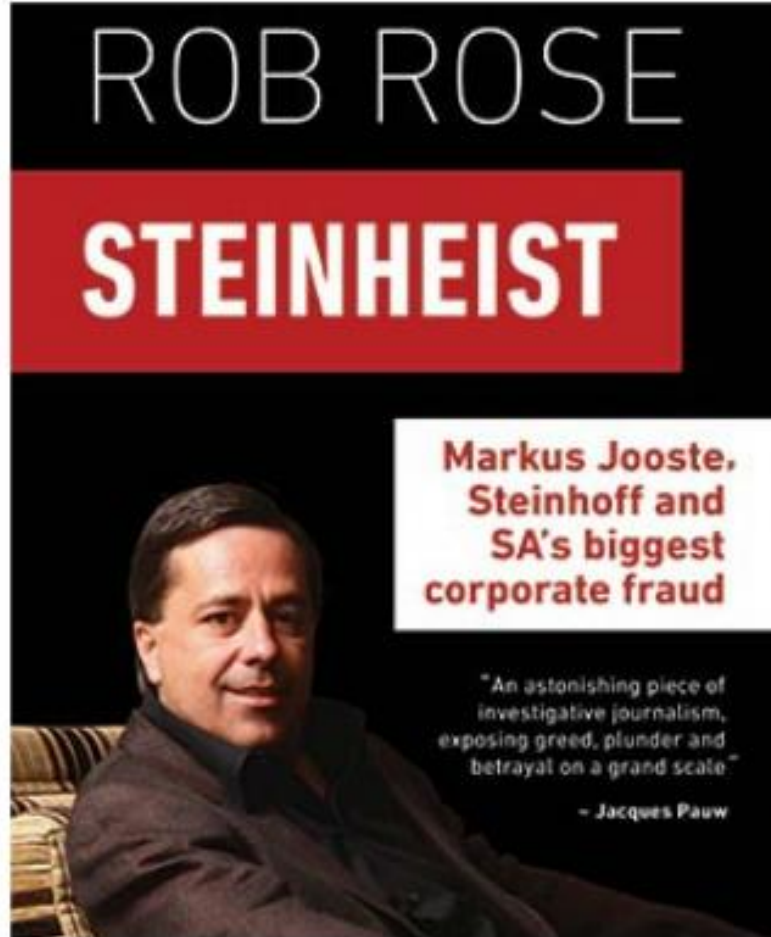
# DUTIES

- **Common law duties**
  - the above;
  - duty not to misappropriate corporate opportunities;
  - duty to account for secret profits;
  - duty to not improperly compete with the company.

# DUTIES

- **Common law duty of care and skill**
  - director must exercise his duties with the degree of skill that may reasonably be expected from a person with his particular knowledge and experience;
  - the skill that he possesses with reasonable care.
- **Duty of care and skill in 2008 Act**
  - a director must act with the care, skill and diligence that may reasonably be expected of someone -
    - fulfilling his functions; and
    - having his knowledge, skill and experience.

Duties and the one still to be prosecuted ... (to date insider trading fine and disciplinary by SAICA pending)



*"CIPC has scolded Telkom CEO Sipho Maseko, ordering him to attend a corporate governance and director duties course" - February 2014*



## DUTIES TO OTHERS

- **Duty owed to the shareholder who appointed him/her?**
  - *Fisheries Development Corporation of SA Ltd V Jorgensen; Fisheries Development Corporation of SA Ltd V AWJ Investments (Pty) Ltd*
    - ❖ "A director is in that capacity not the servant or agent of the shareholder who votes for or otherwise procures his appointment to the board ...
    - ❖ ... (t)he director's duty is to observe the utmost good faith towards the company, and in discharging that duty he is required to –
      - ✓ exercise an independent judgment; and
      - ✓ take decisions according to the best interests of the company as his principal.

## DUTIES TO OTHERS

- **Duty owed to the shareholder who appointed?**
  - *Fisheries Development Corporation of SA Ltd* (cont.)
    - ❖ ... (h)e may in fact be representing the interests of the person who nominated him, and he may even be the servant or agent of that person ...
    - ❖ ... but ... in carrying out his duties and functions as a director, he is in law obliged to serve the interests of the company to the exclusion of the interests of any such nominator, employer or principal.
    - ❖ ... (h)e cannot therefore fetter his vote as a director, save in so far as there may be a contract for the board to vote in that way in the interests of the company, and, as a director, he cannot be subject to the control of any employer or principal other than the company

## DUTIES TO OTHERS

- **Labour representation – Amendment Bill**
  - Shareholder centric / stakeholder centric
  - Other stakeholders



## DUTIES TO OTHERS

- **Another entity in the group / to the group / competitor?**
  - Sitting on board of competing companies / companies with competing interests – once off / ad hoc / continuous;
  - decision in a group context.

## COMMITTEES – IN THE CONTEXT OF DIRECTORS' DUTIES

- **Audit committee**
  - section 94 - does not reduce the functions and duties of the board or the directors of the company, except with respect to the appointment, fees and terms of engagement of the auditor
- **Other board committee (including social and ethics committee)**
  - does not alone satisfy or constitute compliance by a director with the required duty of a director to the company, as set out in section 76

# COMMITTEES – IN THE CONTEXT OF DIRECTORS' DUTIES

- **Remuneration committee**

- Amendment Bill 2018 proposes a gap report; Amendment Bill 2018 proposes remuneration committee resignation if 25% voted against the remuneration report in two consecutive years;
- Amendment Bill 2020 one third resigns and up for re-election if voted against

# CONFLICTS OF INTEREST / CONFLICT OF DUTY

- **Conflict of personal interest**
  - section 75 and the common law.
- **Procedure under section 75**
  - if director or related person has personal financial interest in matter before the board, director must –
    - disclose interest and general nature before matter considered;
    - disclose to meeting any material information known (as defined) to the director;
    - leave meeting after making disclosure, not take part in deliberation;
    - while absent, regarded as present for quorum but not determination.

# CONFLICTS OF INTEREST / CONFLICT OF DUTY

- **Consequences of not disclosing**
  - old position - offence;
  - position under the 2008 Act (section 75) -
    - invalid;
    - unless -
      - ❖ has subsequently been ratified by an ordinary resolution of the shareholders following disclosure of that interest; or
      - ❖ has been declared to be valid by a court.

## CONFLICTS OF INTEREST / CONFLICT OF DUTY

- **Mirror boards / all on board conflicted**
  - possible in law;
  - the section 75(2) exemption does not apply to mirror boards;
  - section 75(3) – if a director is conflicted – shareholder approval;
  - ratification after non-disclosure – not possible if conflict known;
  - are white-wash resolutions possible?

## RELEVANT CASE LAW ON THE 2008 ACT

### ***Visser Citrus Proprietary Limited v Goede Hoop Citrus Proprietary Limited and Others 2014 (5) SA 179 (WCC)***

- requirement in the MOI that the directors must approve a transfer of shares;
- fiduciary duties – best interest of company to refuse;
- fronting; loss of empowerment status.



## CASE LAW

**“A company must not carry on its business recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose”**

- e.g. fronting;
- consequences if breach section 22 of the Companies Act, 2008 – compliance notice, offence, fine;
- consequences as decided in case law – *Rabinowitz v Van Graan and Others 2013 (5) SA 315 (GSJ)*.

## EXAMPLES OF THE COURTS ENDORSING THE KING REPORTS' PRINCIPLES

- **Corporate community has accepted the recommendations of King; conduct of the respondents fly in the face of everything recommended in King and acted irresponsibly, quotes King**

*Minister of Water Affairs & Forestry v Stilfontein Gold Mining Company Ltd and others* (Gauteng, Johannesburg – 2006).

- **King – keep CEO and CFO positions separate**

*Mbethe v United Manganese of /Kalahari (Pty) Ltd* (Gauteng, Johannesburg – 2016).

## EXAMPLES OF THE COURTS ENDORSING THE KING REPORTS' PRINCIPLES

- **Boards of SOC's are enjoined to consider their responsibilities in terms of King IV (and in light of the constitution); integrity is a key principle**  
*SABC v Mpofu and another (Gauteng – 2009).*
- **Division of powers – chairperson v CEO (principal officer); court quotes King II with approval**  
*Council for Medical Schemes vs Selfmed Medical Schemes (Appellate Division – 2010).*

## EXAMPLES OF THE COURTS ENDORSING THE KING REPORTS' PRINCIPLES

- **King IV – keep CEO and CFO positions separate**

*Myburgh v Barinor Holdings (Pty) Ltd and Barinor Management Services (Pty) Ltd (The Labour Court – 2015).*

- **If MOI or shareholders' agreement requires compliance with King IV, there is then a legal obligation**

*Kalahari Resources(Pty) Ltd v Arcelormittal SA and others (Gauteng – 2012).*

# SPECIFIC REQUIREMENTS FOR DIRECTORS RE CORPORATE ACTIONS

## **Issue of shares**

- shareholder approval for issuing of shares to certain persons.

## **Financial assistance**

- shareholder approval;
- solvency and liquidity;
- fair and reasonable.

# SPECIFIC REQUIREMENTS FOR DIRECTORS RE CORPORATE ACTIONS

## **Repurchase**

- special resolution;
- solvency and liquidity.

## **Distributions**

- solvency and liquidity.

**LOANS OR OTHER  
FINANCIAL  
ASSISTANCE TO  
DIRECTORS  
(SECTION 45)**

## R6 million Schindehutte loan could be illegal

Reuters 18 November 2013





## LIABILITY OF DIRECTORS

- **The directors will be liable for any loss, damage, costs (direct or indirect), sustained by the company as regards the non-compliance with certain provisions, if they –**
  - were present at the relevant meeting; or
  - participated (i.e. signed a round robin resolution); and
  - knew about the non-compliance; and
  - failed to vote against the matter.
- **Reeva Forman case (1973 Act)**
  - non-executive director liability – not being at meetings not an excuse.

# LIABILITY OF DIRECTORS

- **Liability in 2008 Act**

- liable for loss, damages and costs suffered pursuant to breaches of duties, MOI and the 2008 Act (to any party);
- joint and several;
- section 218: “Any 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”;
  - 2020 case law (Steinhoff and African Bank) – common law remains that only company can claim from directors (except in special circumstances).

- **Extended standing to apply for remedies**

- class actions (e.g. trade unions).

# BUSINESS JUDGMENT RULE

- **Business judgment rule under the 2008 Act**
  - a director satisfies his duties (regarding information, acting in company's best interests, and care and skill but not good faith and proper purpose) in respect of a particular matter if -
    - he has taken reasonably diligent steps to become informed;
    - he or someone related has no material personal financial interest in the matter, or he complied with section 75 (disclosure); and

# BUSINESS JUDGMENT RULE

- he made a decision, or supported a decision of the board/board committee regarding the matter, and had a rational basis for believing, and did believe, that the decision was in the company's best interests;
- director is entitled to rely on certain persons in exercising his power and performing his functions, e.g. employees he reasonably believes to be reliable, professional advisers and board committees he does not serve on.
- **Fourie NO and others v Newton (1973 Act)**
  - non-executive director liability – CNA board, Edcon nominated.

## BUSINESS JUDGMENT RULE



## INDEMNITY AND INSURANCE

- **The 2008 Act – company may indemnify or take out insurance in favour of a director in respect of any liability unless the liability arises**
  - from wilful misconduct or wilful breach of trust on the part of the director;
  - in respect of a fine imposed on the director due to his conviction of an offence in terms of any national legislation (except in the case of strict liability);
  - where the director knowingly (as defined) –

## INDEMNITY AND INSURANCE

- acted without authority in relation to the company;
- acquiesced in the carrying on of the company's business recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose; or
- was party to an act or omission by the company calculated to defraud a creditor, employee or shareholder of the company, or had another fraudulent purpose.

## COMPLIANCE NOTICES AND ADMINISTRATIVE FINES

- **Only for failure to comply with a compliance notice**
  - Companies Commission;
  - Takeover Panel.
- **Not exceeding the greater of**
  - 10% of the respondent's turnover for the period during which the company failed to comply with the compliance notice; and
  - the maximum prescribed in terms of subsection 175(5)(R1 million).





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