TULANE JOURNAL OF INTERNATIONAL AND COMPARATIVE LAW

VOLUME 26 WINTER 2017 NO. 1

Directors' Liability and Shareholder Remedies in South African Companies—Evaluating Foreign Investor Risk

Peter N. Levenberg SC*

 Peter Levenberg is a Barrister (Advocate) of the High Court of South Africa and a Senior Counsel (the equivalent of a Queens Counsel). He is also a member of the California Bar, having practiced law in California for ten years. Mr. Levenberg currently practices as a trial lawyer in South Africa. He specializes in company law, shareholder disputes, commercial contract disputes, banking and insolvency law, arbitration and mediation. Mr. Levenberg has sat as a High Court judge in South Africa on five prior occasions.

I. INTRODUCTION

You are a New York lawyer advising a U.S.-based multinational corporation that wishes to acquire a majority stake in a South African company. Before investing, your client, as a "*deep pocket*," will want to know what risks the American company and its appointed directors face from claims by the minority shareholder in the South African company or from creditors if the South African company fails.

South African company law is fairly straightforward and largely familiar to Anglo-American lawyers. The primary source of South African corporate law is the New Companies Act 71 of 2008 (the New Companies Act).[1] The New Companies Act builds upon, and partially replaces, prior South African company law that was heavily influenced by earlier English statutes.[2]

The New Companies Act is intended to, among other things, "promote the development of the South African economy by encouraging entrepreneurship and enterprise efficiency and creating flexibility and simplicity in the formation and maintenance of companies."[3] It is also intended to promote transparency and high standards of corporate governance.[4] It seeks to balance the rights of shareholders and directors within companies.[5] Most importantly, it deals quite explicitly with issues relating to directors' liability and shareholder remedies reasonably,

1. Companies Act 71 of 2008 (S. Afr.).
2. *Id.*
3. *Id.* § 7(b).
4. *Id.*
5. *Id.* § 7(i).

clearly, and simply in a manner that takes into account many concerns that have manifested themselves in modern commerce.[6]

South African company law prohibits reckless trading and requires that company directors and majority shareholders observe good corporate governance principles. With certain exceptions, the fiduciary duties of directors in South Africa are similar to those in England and the United States.[7] While majority shareholders have no fiduciary duty to minority shareholders, aggrieved minority shareholders do have flexible and relatively effective statutorily created equitable remedies for oppression.[8]

As a general rule, South African courts will not interfere with the day-to-day management of companies.[9] The overriding principle of South African company law is that majority rule and the company's Constitution prevail where the directors have acted in good faith for a proper purpose and in the best interests of the company.[10]

The exposure of directors and majority shareholders for breach of duty is much more finite than it is in the United States.[11] This is because South African tort law adopts a "sum formula" approach requiring that damages should reflect the actual measure of an aggrieved party's financial loss.[12] Most significantly, South African law does not provide for punitive damages.[13]

This Article examines directors' liability and minority shareholder remedies in South African law and evaluates the potential risk to foreign directors and majority shareholders for breach of duty. Part II analyzes the context and sources of South African contract and tort law. Part III considers the sources of South African company law. Part IV focuses on directors' obligations and potential liability to shareholders and to creditors in the event of a corporate failure. Part V considers the remedies available to oppressed minority shareholders and the risks for majority shareholders who overreach themselves.

---

6. *Id.* § 7(k).

7. FAROUK H.I. CASSIM ET AL., CONTEMPORARY COMPANY LAW 16, 463 (Farouk H.I. Cassim ed., 1st ed. 2011).

8. *See Bayly v. Knowles* 2010 (4) SA 548 (S. Afr.).

9. CASSIM ET AL., *supra* note 7, at 348-49.

10. *Visser Sitrus (Pty) Ltd. v. Goede Hoop Sitrus (Pty) Ltd. & Others* 2014 (5) SA 179 (WCD) at para. 61.

11. J.M. VISSER ET AL., VISSER & POTGIETER, LAW OF DAMAGES 72-73 (J.M. Potgieter, L. Steynberg, T.B. Floyd eds., 3d ed. 2012).

12. *Id.*

13. *See Jones v. Krok* 1996 (1) SA 504 (T) at 515 para. G-H.

II. BASIC PRINCIPLES OF SOUTH AFRICAN COMMON LAW

A. Basic Principles of the South African Common Law and Its Relationship to English Law[14]

South African common law is essentially Roman-Dutch in origin but is influenced by English law, especially where Roman-Dutch law required further development in order to bring it into line with modern economic structures.[15]

In *Rood v. Wallach*,[16] the court held that South African contract law was Roman-Dutch in origin. Accordingly, the English doctrine of consideration does not apply in South African contract law.[17] South Africa, therefore, recognizes that contracts can be entered into without consideration provided that the agreement is "not manifestly impossible, made deliberately and seriously, by persons capable of contracting and having a ground or reason which is not immoral or forbidden by law."[18]

In *Minister of Justice v. Hofmeyr*,[19] the Court held that the South African law of "delict" (tort) is also derived from Roman-Dutch law.

South African property law is based upon Roman law principles with "various traces of Germanic customary law."[20] Accordingly, Anglo-English principles of property law are inapplicable.[21]

---

14. Citations in this Article are mainly to cases reported in various published South African Law Reports, which are obtainable both online and in hard copy. There are also references to certain cases that are not reported in the ordinary Law Reports but appear on sites such as Southern African Legal Information Institute (SAFLII) or Judgments Online (JOL). Cases that have the letters "CC" at the end of the citation are decided by the Constitutional Court. Cases that have the acronym "SCA" are decided by the Supreme Court of Appeal. References to "ZASCA" are to SCA cases reported only on the SCA's website. References to "AD" are references to the Appellate Division, the previous name of the Supreme Court of Appeal.

The Article also contains references to English cases. A reference to *"All ER"* is a reference to the All England Reports. A reference to *"QB"* is a reference to the Queen's Bench.

In addition, there are references to cases decided in the United States and Australia.

15. *Minister of Justice v. Hofmeyr* 1993 (3) SA 131 (AD) at 154-55; *Conradie v. Rossouw* 1919 AD 279; *Rood v. Wallach* 1904 TS 186 at 201; WILLE'S PRINCIPLES OF SOUTH AFRICAN LAW 60-76 (Francios du Bois ed., 9th ed. 2007); H.R. HAHLO & ELLISON KAHN, THE SOUTH AFRICAN LEGAL SYSTEM AND ITS BACKGROUND 590-97(1968).

16. *Rood* 1904 TS at 201.

17. *Id.*

18. *Id.*; *Conradie* 1919 AD at 279.

19. *Hofmeyr* 1993 (3) SA 131 (AD) at 154-155.

20. D.G. KLEYN, SILBERBERG AND SCHOEMAN'S LAW OF PROPERTY 6-7 (P.J. Badenhurst et al. eds., 4th ed. 2003).

21. *Id.* at 7.

The parol evidence rule, which forms part of the South African law of evidence, is derived from English law.[22]

An example of a situation in which South African courts followed English law in order to modernize the Roman-Dutch law is *Haynes v. Kingwilliamstown Municipality.*[23] In that case, the court largely followed English law in analyzing the court's discretion to refuse to grant specific performance of a contract by a defaulting party in circumstances where damages would adequately compensate the plaintiff, it would be difficult for the court to enforce the court's decree, the thing claimed could easily be bought anywhere, or specific performance entailed the rendering of services of a personal nature.[24]

B. South African Law of Tort (Delict)

A tort in South African law is referred to as a "delict."[25] I will use the two terms interchangeably in this Article. A detailed analysis of the South African law of tort is beyond the scope of this Article. However, the basis of delictual liability for those who have a duty of care to others, such as a company director, is relevant to South African company law.[26]

> *One of the most important sections of Roman law that still exists in [South African] law, although time has brought many changes and extensions, relates to liability for patrimonial damage (damnum iniuria datum).*[27] *Roman law in this regard was based on an Act (plebiscitum) from 287 BC known as the lex Aquilia.*[28]

The *Actio Legis Aquilia* evolved over a period of more than 2000 years through the laws of Holland into its present form in South African

---

22. RICHARD HUNTER CHRISTIE & GB BRADFIELD, THE LAW OF CONTRACT IN SOUTH AFRICA 200 (6th ed. 2016) (The parol evidence rule as applied in South Africa *"has long formed a part of the English law of evidence which, subject to the Civil Proceedings Evidence Act 25 of 1995 and the Law of Evidence Amendment Act 45 of 1998, forms the basis of our law of evidence in civil proceedings."*).

23. *Haynes v. Kingswilliamstown Municipality* 1951 (2) SA 371 (AD); *see Farmers' Co-Operative Society (Reg.) v. Berry* 1912 AD 343 at 350.

24. *Haynes* 1951 (2) SA 371 (AD) at 378, 380-81.

25. J. NEETHLING, J.M. POTGIETER, & P.J. VISSER, THE LAW OF DELICT 6 (J.C. Knobel ed., 5th ed. 2006).

26. CASSIM ET AL., *supra* note 7, at 505.

27. Monetary damage. *Damnum iniuria datum*, BLACK'S LAW DICTIONARY (10th ed. 2014).

28. NEETHLING ET AL., *supra* note 25, at 7.

law.[29] In *Coronation Brick (Pty) Ltd. v. Strachan Construction Co. (Pty) Ltd.*,[30] the court held:

> The legal basis of the plaintiff's claim is the *lex Aquilia*. In essence the Aquilian action lies for patrimonial loss caused wrongfully (or unlawfully) and culpably. Although the contrary view has long been held by many authorities, it seems clear that the fact that the patrimonial loss suffered did not result from physical injury to the corporeal property or person of the plaintiff, but was purely economic, is not a bar to the Aquilian action.[31]

Although there was doubt during the first half of the twentieth century concerning whether the Aquilian action was available for negligent misrepresentation causing pure economic loss, South African courts laid this controversy to rest in 1979.[32] It is now settled law that an action lies for negligent misrepresentation resulting in pure economic loss.[33]

In *Mukheiber v. Raath*,[34] the test for negligence under the South African *lex Aquilia* was enunciated as follows:

> [31] In our law, the standard of conduct expected from all members of society is that of the *bonus paterfamilias, i.e.* the reasonable man or woman in the position of the defendant. An act which falls short of this standard and which causes damage unlawfully is described as negligent; *i.e.* it is tainted with *culpa*.[35]
>
> The test for *culpa* can, in the light of the development of our laws since *Kruger v. Coetzee* 1966 (2) SA 428 (A) be stated as follows . . .
>
> For the purpose of liability *culpa* arises if—
>
> (a) a reasonable person in the position of the defendant—
>
> (i) would have foreseen harm of the general kind that actually occurred;
>
> (ii) would have foreseen the general kind of causal sequence by which that harm occurred;
>
> (iii) would have taken steps to guard against it, and
>
> (b) the defendant failed to take those steps.

---

29. VISSER, *supra* note 11, at 7-11.

30. *Coronation Brick, (PTY) Ltd. v. Strachan Construction Co. (PTY) Ltd.* 1982 (4) SA 371 (D&CLD) at 377.

31. *Admin., Natal v. Trust Bank van Afrika Bpk* 1979 (3) SA 824 (A) at 830 H-831 B; *Greenfield Eng'g Works (Pty) Ltd v. NKR Construction (Pty) Ltd* 1978 (4) SA 901 (N) at 913B-917D.

32. *Mukheiber v. Raath* 1999 (3) SA 1065 (SCA); *Standard Chartered Bank of Canada v. Nedperm Bank Ltd* 1994 (4) SA 747 (A); *Admin., Natal* 1979 (3) SA 824 (A).

33. NEETHLING ET AL., *supra* note 25, at 10 (citing *Admin., Natal* 1979 (3) SA 824 (A)).

34. *Mukheiber* 1999 (3) SA 1065 (SCA) at paras. 31-32.

35. Negligence. *Culpa*, BLACK'S LAW DICTIONARY (10th ed. 2014).

> [32] In the case of an expert, such as a surgeon, the standard is higher than that of the ordinary lay person and the court must consider the general level of skill and diligence possessed and exercised at the time by the members of the branch of the profession to which the practitioner belongs.[36]

In *Van Wyk v. Lewis*,[37] the Court considered the standard of care required from a medical practitioner and stated:

> "[A] medical practitioner is not expected to bring to bear upon the case entrusted to him the highest possible degree of professional skill, but he is bound to employ reasonable skill and care." In deciding what is reasonable the Court will have regard to the general level of skill and diligence possessed and exercised at the time by the members of the branch of the profession to which the practitioner belongs.[38]

This standard of skill and care is relevant when analyzing the degree of skill and care required of a company director. A company director is required to exercise the degree of care, skill, and diligence that may reasonably be expected of a person carrying out that director's functions. However, he is also required to exercise the degree of skill and care that would be expected of a person with his knowledge, skill, or qualifications.[39]

South African law does not penalize every negligent act or omission.[40] The act or omission must also be unlawful in the sense that the court, through the application of public policy, recognizes that the person who committed the act or omission had a legal duty of care to the person harmed by the act or omission.[41]

As analyzed in Part IV below, the liability of a director to his company for negligent acts derives from common law and statute.[42] The question of whether the directors will incur liability to individual shareholders for negligent or reckless conduct is in large part governed by the law of delict, which requires that a negligent act or omission must

---

36. *Mukheiber* 1999 (3) SA 1065 (SCA) at paras. 31-32.
37. *Van Wyk v. Lewis* 1924 AD 438 (SCA) at 444.
38. *Id.*
39. Companies Act 71 of 2008 § 76(3); *Fisheries Dev. Corp. of SA Ltd. v. Jorgensen & Another Fisheries Dev. Corp. of SA Ltd. v. AWJ Inv. (PTY) Ltd. & Others* 1980 (4) SA 156 (W)at 165 F.
40. *Mukheiber v. Raath* 1999 (3) SA 1065 (SCA) at para. 25.
41. *Tr.s, Two Oceans Aquarium Trust v. Kantey & Templer (Pty) Ltd* 2006 (3) SA 138 (SCA) at para. 10; *Mukheiber v. Raath & Another* 1999 (3) SA 1065 (SCA) at para. 25; *Standard Chartered Bank of Canada v. Nedperm Bank Ltd.* 1994 (4) SA 747 (A) at 769-73 D.
42. *See* Companies Act 71 of 2008 § 76.

take place in a context in which there is a legal obligation to take care in relation to the aggrieved party.

C. The Measure of Damages in Tort

A natural consideration for multinational companies investing in South Africa is whether the company or the directors might be exposed to excessive damages claims in South Africa for breach of duty.[43] Subject to certain statutory exceptions,[44] South African common law does not allow a plaintiff to recover damages in excess of the plaintiff's proven monetary loss.[45] Damages in delict are "wholly compensatory."[46]

South African courts require that damages be proven with a reasonable amount of precision; that is to say they adopt a "sum formula" approach.[47] This has been described in *Visser and Potgieter: Law of Damages*[48] as follows:

> In terms of the sum-formula doctrine damage is the negative difference between a person's current patrimonial[49] position (after the occurrence of the damage-causing event) and his or her patrimonial position which would hypothetically have existed if the damage-causing event had not taken place. This means that an actual current patrimonial *sum* is compared with a hypothetical current patrimonial *sum*. This explains the concept *sum-formula* approach.
>
> The measure of damage and damages in delict is known as 'negative interesse': this refers to the calculation of an amount of money which is necessary to place someone in the (hypothetical) financial position he or she would have enjoyed had a delict not been committed.[50]

In the seminal case of Union Government (*Minister of Railways & Harbours v. Warneke*),[51] the Appellate Division held:

> And we are at once faced with the fact that it was essential to a claim under the *lex Aquilia* that there should have been actual *damnum* in the sense of

---

43. NEETHLING ET AL., *supra* note 25, at 6.

44. Companies Act 61 of 1973 § 424, which provides that, where the "business of a company was or is being carried on recklessly or with intent to defraud," parties to that conduct may be held liable for all of the debts of the company without the need to prove that the recklessness or fraud caused loss to the creditors. This section is analyzed in more detail below.

45. *Dippenaar v. Shield Ins. Co.* 1979 (2) SA 904 (A) at 907 C.

46. *Id.* at 916 H-917 D.

47. VISSER ET AL., *supra* note 11, at 72-73.

48. *Id.*

49. Financial loss. *Patrimonial*, BLACK'S LAW DICTIONARY (10th ed. 2014).

50. VISSER ET AL., *supra* note 11, at 72-73.

51. *Union Government (Minister of Railways & Harbours) v. Warneke* 1911 AD 657 at 665.

> loss to the property of the injured person by the act complained of . . . . In later Roman law property came to mean the *universitas* of the plaintiff's rights and duties, and the object of the action was to recover the difference between that *universitas* as it was after the act of damage, and as it would have been if the act had not been committed.[52]

Accordingly, any damages claimed for breach of fiduciary duty or other wrongdoing should reflect the actual measure of an aggrieved party's financial loss.[53] However, the courts may employ a small element of guesswork where the best evidence available as to damages is insufficient to deal with all contingencies.[54]

A significant factor that reduces the risk to foreign companies and directors investing in South African companies is that South African law does not allow the award of punitive damages.[55] In *Jones v. Krock*,[56] the court held:

> It is the policy of South African law and practice that for breach of contract the injured party is entitled to no more than compensation for the damages

---

52. *Rudman v. Road Accident Fund* 2003 (2) SA 234 (SCA) at paras. 10-11 (holding that where a plaintiff claimed damages for bodily injuries incurred in a motor vehicle accident he could claim for loss of earnings but only to the extent that such loss diminished his estate or patrimony. The court concluded that the plaintiff's diminished earning capacity was proved but that the evidence did not go further and prove that his incapacity constituted a loss which had diminished his estate. Rudman's ability to prove that his estate had suffered actual patrimonial loss was in this case severely hampered by the fact that his entire business was housed in a company and he was unable to prove that the company lost business as a direct result of his injuries); *Dippenaar v. Shield Ins. Co.* 1979 (2) SA 904 (A) at 916 H-917 D; *Union Government* 1911 AD 657 at 665.

53. *Dippenaar* 1979 (2) SA 904 (A) at 907 C.

54. *Hushon v. Pictech* 1997 (4) SA 399 (A) at 412 C-H (The plaintiff claimed damages for unlawful competition where the defendant had been involved in a plot to destroy the plaintiff's business and divert a major business opportunity relating to imported air conditioning equipment from the plaintiff to the defendant. As the business opportunity was diverted from the plaintiff before the plaintiff had managed to get the new business off the ground, the plaintiff had no comparative evidence reflecting the plaintiff's profits before and after the tort was committed. The plaintiff asserted that the profits that the defendant had made out of the enterprise was the best measure of the plaintiff's loss. However, the court held that the defendant was a much larger company and would likely have made a greater success of the business. Taking into account all the evidence and the contingencies, the court estimated that the plaintiff's damages should be assessed at a percentage of the defendant's profits); *Caxton Ltd. & Others v. Reeva Forman (Pty) Ltd . & Another* 1990 (3) SA 547 (A) at 573 D-J (The court had to assess the damages suffered by the plaintiff's business as a result of the defendant's libel. The plaintiff had not been able to demonstrate that its loss of profits was not in part attributable to a severe economic recession that had occurred after the libel had taken place. In that context, the court decided to "do the best it [could] on the material available . . . ."); *ESSO Standard SA (Pty) Ltd. v. Katz* 1981 (1) SA 964 (A) at 969 H- 970 H.

55. *Jones v. Krok* 1996 (1) SA 504 (T) at 515 G-H.

56. *Id.*

> actually suffered by him. The *quantum* is not in any way dependent upon, or influenced by, the reprehensible behaviour of the defendant or the flagrancy of the breach . . . .[57] The same applies to the assessment of the *quantum* of damages under the *lex Aquilia* . . . .[58] It is thus trite that the award of punitive damages in such instances, in which category falls the award in this case, is alien to our legal system.[59]

In *Jones v. Krok*, the court refused to enforce that portion of a judgment that had been obtained against a defendant in California that was for punitive damages.[60] The court held that it could not put its imprimatur on an award of damages for reprehensible behavior where the court would effectively be allowing the plaintiff double damages for the patrimonial loss suffered.[61] The court held that such an award was *"so excessive and* exorbitant that . . . it is contrary to the public policy in this country."[62]

D. Equity and Good Faith in South African Law

Generally speaking, South African courts are not courts of equity and are not empowered to apply equitable principles.[63] However, where the common law or statute specifically calls for or contains an equitable principle, the court will be empowered to employ that concept.[64]

In *Weinierlien v. Goch Buildings Ltd.*[65] the court held:

> In the earlier case of *Mills & Sons v Benjamin Bros.* (1976, BUCH. at 121) the same learned judge observed: "Now it is quite true that this Court is a Court of Equity only insofar as it is consistent with the principles of Roman-Dutch law." This qualification is of importance, for equity cannot and does not override a clear provision of our law. Our common law, based to a great extent on the civil law, contains many an equitable principle; but equity, as distinct from and opposed to the law, does not prevail with us.

---

57. *Admin., Natal v. Edouard* 1990 (3) SA 581 (A) at 597.
58. *Santam Versekeringsmaatskappy Bpk v. Byleveldt* 1973 (2) SA 146 (A) at 152 H.
59. *Jones*, 1996 (1) SA 504 (T) at 515 G-H.
60. *Id.* at 515-16.
61. *Id.*
62. *Id.* at 517 G.
63. *Weinerlein v. Goch Bldgs. Ltd.* 1925 AD 282 at 295.
64. *See Brisley v. Drotsky* 2002 (4) SA 1 (SCA) at para. 9 (The defendant was held bound by an *"entrenchment clause"* in a written contract that provided that there could be no amendments to the contract, or cancellation thereof unless they complied with specific formalities. The defendant sought to avoid the consequences of the entrenchment clause because it was in the circumstances, unreasonable, unfair and in conflict with the principles of *bona fides*. The court held that it could not apply equitable principles or principles of *bona fides* to allow the defendant to escape the consequences of his bargain).
65. *Weinierlien* 1925 AD at 295.

> Equitable principles are only of force insofar as they have become authoritatively incorporated and recognized as rules of positive law.[66]

This distinction is important in evaluating directors' liability and shareholders' remedies because, in that context, the equitable remedies that the court can grant are usually limited to those that are expressly provided for in the corporate statute.[67]

It is also theoretically a principle of South African law that all contracts are contracts of good faith.[68] In *Meskin v. Anglo American Corporation of SA Ltd.*,[69] the court held:

> It is now accepted that all contracts are *bonae fidei*[70] (some are even said to be *uberrimae fidei*[71]). This involves good faith (*bonae fides)* as a criterion of interpreting a contract . . . and in evaluating the conduct of the parties both in respect of its performance . . . and of its antecedent negotiation. Where a contract is concluded the law expressly invokes the dictates of good faith, and conduct inconsistent with those dictates may in appropriate circumstances be considered to be fraud . . . .[72]

In *Neugebauer & Co. Ltd. v. Hermann*, Chief Justice Innes held:

> The American authorities [with respect to sales] are discussed and in Benjamin On *Sales* (5th ed. p465). Our law accords, in my opinion, more with the American than with the English view. It is not so much a question of public policy as of the requirements of good faith.
>
> The principle is fundamental that *bona fides* is required from both parties to a contract of sale.[73]

However, while lip service is paid to the notion that all contracts are contracts of good faith, this concept has only limited enforceable content in our law.[74] It has mostly been applied to enable an aggrieved party to resile from a sale or claim damages where good faith required disclosure of a particular fact.[75]

---

66. *Id.*

67. *See*, *e.g.*, Companies Act 71 of 2008 § 163 (affording the court a wide equitable discretion to address oppression of a minority shareholder or a director of a company).

68. *Meskin v. Anglo American Corporation of SA Ltd.* 1968 (4) SA 793 at 802 A-C.

69. *Id.*

70. Good faith. *Bonae fidei*, BLACK'S LAW DICTIONARY (10th ed. 2014).

71. The utmost good faith. *Uberrimae fidei*, BLACK'S LAW DICTIONARY (10th ed. 2014).

72. *Meskin* 1968 (4) SA 793 at 802 A-C.

73. *Neugebauer & Co. Ltd. v. Hermann* 1923 AD 564 at 573-74..

74. *Dibley v. Furter* 1951 (4) SA 73 (C) at 85.

75. *See id.* (The plaintiff purchased a property for residential purposes. After the sale, the plaintiff discovered that, to the knowledge of the seller, there was a graveyard on a portion of the ground sold. The court found that the seller had fraudulently concealed this fact from the purchaser and accordingly set aside the contract).

Accordingly, the doctrine of good faith in contract has little impact in dealings between directors and shareholders or majority shareholders and minority shareholders outside of contracts of sale of shares, except where a statute expressly makes it relevant.[76]

III. SOURCES OF SOUTH AFRICAN COMPANY LAW GOVERNING RELATIONSHIPS BETWEEN SHAREHOLDERS AND DIRECTORS

A. Sources of Company Law

South African company law is heavily influenced by English company law. "The first Southern African Companies Act, the Cape Joint Stock Companies Limited Liability Act of 1861, was based on earlier English company legislation."[77] Similarly, the first South African Companies Act that was enacted after South Africa became the Union of South Africa, the South African Companies Act 46 of 1926, was also based on English statutory law.[78] As the South African company law was largely based on English company law, the "inner common law of companies," being the courts' decisions interpreting sections of the Companies Act, was also based upon English law.[79]

While English judicial decisions in connection with the Companies Act are not binding on South African courts, they are afforded great deference.[80] However, when looking at English precedents, differences in the respective legal systems and statutes must be taken into account.[81] In 2008, the New Companies Act was passed, which modified some of the English law concepts.[82] This Act also provides for business rescue, which is similar to Chapter 11 of the U.S. Bankruptcy Code.[83] Additionally, the Act that preceded the New Companies Act was the Companies Act 61 of 1973 (the Old Companies Act).[84] This was based more closely upon prior English companies acts than the 2008 Act.[85]

---

76. *See*, *e.g.*, Companies Act 71 of 2008 §§ 163 (Relief from oppression), 77 (Liability of directors and prescribed officers).

77. 4 THE LAW OF SOUTH AFRICA 7 (W.A. Joubert & J.A. Faris eds., 2d ed. 2013).

78. *Id.*

79. *Id.*

80. *Id.*; CASSIM ET AL., *supra* note 7, at 10.

81. 4 THE LAW OF SOUTH AFRICA, *supra* note 77.

82. *See* Companies Act 71 of 2008 §§ 1-225 (See change in text p.25. It is an implication by comparing the whole of both Acts. But it is beyond the scope of this Article to do that comprehensively.).

83. *Id.* §§ 128-155; *cf.* 11 U.S.C. §§ 1121-1129.

84. *See* Companies Act 61 of 1973, ch. 1, §§ 2-4.

85. HAHLO & KAHN, *supra* note 15, at 594.

The New Companies Act did not repeal the Old Companies Act in every respect.[86] In terms of schedule 5, article 9 of the New Companies Act, Chapter 14 of the Old Companies Act continues to apply with respect to the winding-up (liquidation) of insolvent (i.e., bankrupt) companies.[87] Of particular importance to this Article is the fact that section 424 of the Old Companies Act remains in full force and effect with regard to insolvent companies.[88] That section, which will be analyzed in more detail below, affords a remedy to creditors, shareholders, or liquidators (corporate bankruptcy trustees) of an insolvent company against directors and others who were party to carrying on the business of the bankrupt company recklessly or with intent to defraud creditors of the company.

Section 5(2) of the New Companies Act expressly provides that a court can, in interpreting or applying the Act, "consider foreign company law."[89] While the New Companies Act states this expressly, the South African courts have in any event over the past century looked to other jurisdictions, especially to England, when interpreting unclear portions of the statutory company law.[90] Section 7 of the New Companies Act provides that:

> The purpose of this Act is to—
> (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 mean 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; . . . .

86. *See* Companies Act 71 of 2008.
87. *Id.* § 5(9).
88. *Id.*
89. *Id.* § 5(2).
90. *See*, *e.g.*, *Sage Holdings Ltd. v. The Unisec Group Ltd. & Others* 1982 (1) SA 337 (W) 385 A; *Fisheries Dev. Corp. of SA Ltd. v. Jorgensen & Another Fisheries Dev. Corp. of SA Ltd. v. AWJ Invs. (PTY) Ltd. & Others* 1980 (4) SA 156 (W) 165 F; *Robinson v. Randfontein Estate Gold Mining Co.* 1921 AD 168 at 177-80.

> (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 . . . .[91]

One of the most significant innovations in the New Companies Act is that, while all companies were previously required to prepare audited annual financial statements within six months after the end of their financial year, a company whose activities do not exceed a certain size threshold is now not required to have those financial statements audited.[92] As a practical matter, it is unlikely that subsidiaries of large foreign multinationals will be exempt from preparing audited annual financial statements because their size is likely to exceed the thresholds referred to above.[93] In any event, multinationals will probably be required to ensure that the financial statements of the local subsidiary are audited in order to comply with reporting requirements in the foreign jurisdiction in which the holding company is incorporated.[94]

Another important provision that promotes flexibility is sections 6(8)(a) and (b), which provide that, where a form of document, record, statement, or notice is prescribed in terms of the New Companies Act for any purpose, it is not necessary to use the exact form.[95] Substantial compliance with the Act will usually be sufficient.[96] Additionally, another important change is that the capital maintenance rule, which required that the issued share capital of a company remain as a permanent fund for the payment of claims of the company's creditors, has largely fallen away.[97] The only limitations on capital distributions—whether through dividends or the purchase by a company of its own shares—that remain are those that prevent a company from making distributions to its shareholders, unless the company has passed the solvency and liquidity test.[98]

---

91. Companies Act 71 of 2008 § 7.
92. *Id.* § 30; Regulations to the Companies Act (the Regulations) §§ 26, 28.
93. *See* Companies Act 71 of 2008 § 30.
94. *See id.*
95. *See id.*
96. *Id.* § 8(a)-(b).
97. CASSIM ET AL., *supra* note 7, at 10.
98. Companies Act 71 of 2008 §§ 41, 46.

Another feature of the New Companies Act is there has been an attempt to draft it in plainer, less legally arcane language than the prior Companies Act.[99] This approach will become apparent when we examine specific sections of the Companies Act below. In my opinion, the New Companies Act has in many instances achieved its goal of clarity but not all provisions are entirely clear.[100]

B. The Company's Constitution and Shareholder Agreements

The constitution of a South African company is set out in its memorandum of incorporation (the MOI).[101] Under the Old Companies Act, a company's constitution was to be in two separate documents—one being the memorandum of association and the other being the articles of association.[102] The use of one document simplifies the procedure for the company's constitution. "A company's memorandum is binding between the company and each shareholder, between or among the shareholders of the company, and between the company" and each member of the board or any other person serving as a member of the committee of the board.[103]

The MOI "must be consistent with the New Companies Act and is void to the extent that it contravenes, or is inconsistent with," the New Companies Act.[104] Subject to that proviso, there is considerable flexibility in what can be contained in an MOI. It can include provisions "dealing with any matter that [the New Companies] Act does not address; or altering the effect of any alterable provision of [the New Companies] Act," or imposing on the company a higher standard, greater restriction, longer period of time, or any similarly more onerous commitment than would otherwise apply to the company in terms of an alterable provision of the New Companies Act.[105] It may also contain stricter "conditions applicable to the company, and any requirement for the amendment of any such condition."[106]

The MOI and any amendments thereto must be filed with the Companies and Intellectual Property Commission (CIPC), which is the entity ultimately responsible for the administration of companies in

99. *Id.*
100. *See id.* § 6 (dealing with business rescue).
101. *Id.* § 15.
102. Companies Act 61 of 1973 §§ 52-62.
103. Companies Act 71 of 2008 § 15(6).
104. *Id.* § 15(1).
105. *Id.* § 15(2)(a).
106. *Id.* § 15(2)(b).

South Africa.[107] The MOI is a public document.[108] However, as a practical matter, it can take weeks for a member of the public, who is not a shareholder, to obtain a copy of the MOI from CIPC.[109] Shareholders can obtain a copy of the MOI more expeditiously within fourteen business days directly from the company.[110]

As a consequence of the difficulty in obtaining a copy of the MOI expeditiously from CIPC, all shareholders, both majority and minority, are well-advised to ensure that they have copies of the MOI in their possession.[111] I have seen foreign majority shareholders, who have left the administration of their company in the hands of local minority shareholders with whom they have later fallen out, experience difficulty in obtaining a copy of the MOI as a prelude to bringing proceedings to enforce their rights. The shareholders can also enter into agreements with each other concerning any matter relating to the company.[112] However, to the extent that that agreement is inconsistent with the New Companies Act or the MOI, it is void to the extent of the inconsistency.[113] In short, the shareholders cannot contract out of the mandatory provisions of the New Companies Act or enter into a backroom agreement that conflicts with the public document (i.e., the MOI) that has been registered with CIPC.[114]

As the New Companies Act affords considerable flexibility in what the parties can insert into the MOI, I usually advise clients to ensure that all important governance issues between them are set out in the MOI. However, there may be some rights and obligations that the shareholders wish to incorporate in a document that is not a public document, such as, for example, a clause that permits one party an option to: (1) put its shares to the other party; or (2) call the shares of the other party on the happening of certain conditions.[115] Additionally, an arbitration agreement can be inserted in both an MOI and a shareholders' agreement.[116] However, to the extent that a dispute that arises between shareholders is

---

107. *Id.* §§ 13, 16.

108. CASSIM ET AL., *supra* note 7, at 102-03, 122.

109. *CPIC: Service Delivery Standards—Our Promise to our Customers*, COMPANIES & INTELL. PROP. COMMISSION 4 (2016), http://www.cipc.co.za/files/8414/7437/7256/Companies__CC__and_Directors.pdf.

110. Companies Act 71 of 2008 § 27.

111. *See id*; CASSIM ET AL., *supra* note 7, at 117, 119.

112. CASSIM ET AL., *supra* note 7, at 131.

113. Companies Act 71 of 2008 § 15(7).

114. *Id.*

115. CASSIM ET AL., *supra* note 7, at 118, 137-38.

116. *Id.* at 772-73; Companies Act 71 of 2008 § 156(a).

one that can be resolved only by a court, rather than an arbitrator, the parties will have to proceed in court on that dispute.[117]

It is common for shareholders to include in their shareholder agreement a provision that the parties will act in the utmost good faith towards each other but will not be considered to be partners.[118] As all South African contracts are, as noted above, theoretically contracts of good faith, this clause has no real enforceable content.[119] The duty of good faith between shareholders is better enforced through the minority shareholder protections of section 163 of the New Companies Act.[120]

IV. DIRECTORS' LIABILITY AND OBLIGATIONS

Under South African common law, directors owe a fiduciary duty as well as a duty of skill and care to the company.[121]

A. The Nature of the Directors' Fiduciary Duties

Under South African common law, a director's fiduciary duties are largely circumscribed by English law, although the English law is also underscored by general Roman-Dutch legal principles.[122] In *Robinson v. Randfontein Estate Gold Mining Co. Ltd.*,[123] the court considered the remedies available to a company whose director acquired for himself a corporate opportunity that properly belonged to the company.[124] The court stated:

> Where one man stands to another in a position of confidence involving a duty to protect the interests of that other, he is not allowed to make a secret profit at the other's expense or place himself in a position where his

117. *See Peel v. Hamon J & C Eng'g (Pty) Ltd.* 2013 (2) SA 331 (SGHC) at para. 68 (holding that an arbitrator did not have the power to grant relief to an oppressed minority shareholder under section 163 of the Companies Act as that section conferred that power only upon a court).

118. *Shareholders' Agreement Between Tronox Ltd., Exxaro Resources Ltd., Exxaro Sand Proprietary Ltd., and Exxaro TSA Sand Proprietary Ltd.*, U.S. SEC. & EXCHANGE COMMISSION § 21.8, https://www.sec.gov/Archives/edgar/data/1530804/000119312512277246/d369573dex102.htm (last visited Nov. 13, 2017).

119. *Meskin v. Anglo American Corporation of SA Ltd.* 1968 (4) SA 793 at 802 A-C.

120. Companies Act 71 of 2008 § 163.

121. *Fisheries Dev. Corp. of SA Ltd. v. Jorgensen & Another Fisheries Dev. Corp. of SA Ltd. v. AWJ Invs. (PTY) Ltd. & Others* 1980 (4) SA 156 (W) at 165 F-166 E; *Robinson v. Randfontein Estates Gold Mining Company Co.* 1921 AD 168 at 177-78; CASSIM ET AL., *supra* note 7, at 467; 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 176 para. 129.

122. *Robinson* 1921 AD 168 at 177-80.

123. *Id.*

124. *Id.*

> interests conflict with his duty. The principle underlies an extensive field of legal relationships. A guardian to his ward, a solicitor to his client, an agent to his principal, afford examples of persons occupying such a position. As was pointed out in the *Aberdeen Railway Company v. Blaikie Bros.* (1 Macqueen 474), the doctrine is to be found in the civil law (*Digest 18.1. 34.7*)[125] and must of necessity form part of every civilized system of jurisprudence. It prevents an agent from properly entering into any transaction which would cause his interests and his duty to clash. If employed to buy, he cannot sell his own property; if employed to sell, he cannot buy his own property; nor can he make any profit from his agency save the agreed remuneration; all such profit belongs not to him, but to his principal. There is only one way by which such transactions can be validated, and that is by the free consent of the principal following upon a full disclosure of the agent. In such a case the special relationship *quoad* that transaction falls away and the parties deal at arm's length with one another. The general doctrine is clear enough; but the remedies available to a principal who discovers that he has purchased his agent's own property depends upon considerations of some nicety. Obviously, he is not bound by the contract unless he chooses; he may elect therefore to repudiate or confirm it. But, if he wishes it to stand and also claims the resulting profit, he must show that such profit arises from transactions completely covered by the prohibitive operation of the relationship. That is a point which may be conveniently considered in connection with the more recent English decisions regarding sales by directors. A director is, of course, an agent; generally, he acts in conjunction with his co-directors; but he may be duly authorized to act alone, and like any other agent, he may without antecedent authority, place himself in such a position that a Court will not allow him to say that he did not so act.[126]

As a director's fiduciary duty at common law is essentially determined based on English legal principles, the obligations of a director of the company are familiar to Anglo-American lawyers.[127] In this respect, the language of a former South African Chief Justice, Rose Innes, resonates with the language of the Supreme Court of Delaware in *Guth v. Loft Inc.*[128] Guth was the president and dominant personality in Loft Inc., a corporation that engaged in the manufacturing and selling of candies, syrups, beverages, and foodstuffs.[129] In 1931, Coca-Cola was

---

125. This is in Roman and Roman-Dutch law and the reference is to *The Digest* of the Roman Emperor Justinian.

126. *Robinson* 1921 AD 168 at 177-80.

127. Guth v. Loft, 5 A.2d 503, 510 (Del. 1939).

128. *Id.* at 505.

129. *Id.*

dispensed at all of the Loft stores. Guth was dissatisfied with the prices that Coca-Cola was charging.[130] Guth then secured an opportunity to acquire Pepsi Cola.[131] After he had acquired Pepsi Cola, Guth caused Loft to replace Coca-Cola with Pepsi.[132] Loft also provided financing for Pepsi.[133] The Delaware Supreme Court granted Loft's suit to impress a trust on all of the shares of stock in the Pepsi Cola company registered in the name of Guth.[134]

In the process of delivering the judgment, Delaware Chief Justice Layton stated:

> Corporate officers and directors are not permitted to use their position of trust and confidence to further their private interests. While technically not trustees, they stand in a fiduciary relation to the corporation and its stockholders.[135] A public policy, existing through the years, derived from a profound knowledge of human characteristics and motives, has established a rule that demands of a corporate officer or director, peremptorily and inexorably, the most scrupulous observance of his duty, not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ability might properly bring to it, or to enable it to make in the reasonable and lawful exercise of its powers. The rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest. The occasions for the determination of honesty, good faith and loyal conduct are many and varied, and no hard and fast rule can be formulated. The standard of loyalty is measured by no fixed scale.[136]

As it appears in *Robinson v. Randfontein Estates*, it is not impossible for a director to acquire assets or an interest in the same field in which the company operates.[137] The director is only liable for a breach of duty where he acquires or sells property, in which the company might be interested where he is specifically charged with buying or selling that property.[138] An example of the application of this principle can be found

---

130. *Id.* at 506.
131. *Id.* at 507.
132. *Id.* at 506.
133. *Id.* at 508.
134. *Id.* at 510.
135. As appears from what is more fully set forth below, a South African company director owes a fiduciary duty only to the company and not to the stockholders.
136. *Guth*, 5 A.2d at 510.
137. *Robinson v. Randfontein Estates Gold Mining Company Ltd.* 1921 AD 168 at 178.
138. *Id.*

in *Bellairs v. Hodnett & Another.*[139] Bellairs was an experienced real estate developer.[140] He invited Hodnett to enter into a partnership with him for the development of a township in Northcliff, Johannesburg, in South Africa known as "N.15."[141] A company was formed as the vehicle for the partnership.[142] The company then acquired an additional adjacent property, "N.19."[143] Bellairs subsequently acquired a further adjacent property for himself, "N.20."[144] Hodnett maintained that Bellairs' fiduciary obligation was to acquire the property for the company.[145] The court rejected Hodnett's suit on the basis that the parties had never agreed to develop any further properties together beyond the two that they had acquired in the name of the company—N.19 and N.15.[146]

The court held:

> On the evidence, as a whole it seems clear that Hodnett and Bellairs embarked upon a limited joint venture—the developing of N.15. By subsequent agreement that was enlarged to include N.19—but to that extent it remained a limited venture. Mere "loose talk" could not enlarge its ambit. It follows that the scope of the business of the Company, the machinery employed, did not transcend the limited scope.[147]

Even where the director has a conflict of interest, the transaction that took place can be validated "*by the free consent of the principal following upon a full disclosure of the agent*."[148]

At common law, the general rule is that disclosure must be made to the members in general meeting, and only they have the power to approve the contract.[149] However, where the directors also effectively control the voting rights of the shareholders, the transaction must be approved by all of the shareholders and not simply a majority.[150] Otherwise, directors would in effect be able to perpetrate a fraud upon

---

139. *Bellairs v. Hodnett & Another* 1978 (1) SA 1109 (A) at 1132 H-1133 G.
140. *Id.* at 1131.
141. *Id.* at 1132.
142. *Id.*
143. *Id.*
144. *Id.* at 1132.
145. *Id.* at 1133.
146. *Id.*
147. *Id.*
148. *Id.* at 1132 E.
149. Neptune (Vehicle Washing Equip.) Ltd. v. Fitzgerald (1995) 3 All ER 811, 814; Guinness PLC v. Saunders (1988) 2 All ER 940 (CA) (Eng.); Imperial Mercantile Credit Ass'n v. Coleman (1871) 6 Ch 558, 567-68 (Eng.); *African Claim and Land Co. v. WJ Langermann* 1905 TS 494 at 523; 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 217.
150. 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 217.

the company.[151] In any event, a minority shareholder who did not approve of the transaction would probably also be able to obtain relief today from this oppressive conduct under section 163 of the New Companies Act.[152]

Directors could deal with the company at common law provided that the director broke off his or her relationship with the company in its entirety for the purposes of that particular transaction, acted openly and in good faith, and dealt with the company at arm's length.[153] This rule is known as the "fair dealing rule."[154] *Joubert* summarizes the fair dealing rule as follows:

> The primary duty that the common-law fair-dealing rule imposes on the director is that of disclosing his or her interest in the contract. However, the director must also:
> (a) correct any material misstatements which he or she may have made in the negotiations, or otherwise, which would or might have a bearing on the company's decision to enter into the contract;
> (b) answer truthfully any questions which are put to him or her about matters which would or might have a bearing upon the contract;
> (c) disclose, unasked, any information that he or she acquired when acting for the company which is likely to influence the company's decision and which he or she knows that those acting on its behalf do not already possess.[155]

Section 75 of the New Companies Act deals with the directors' obligations to make disclosure of his personal financial interests.[156] The meaning of the section and its effect upon the common law is well-summarized in *Kensal Rise Investments (Pty) Ltd. v. Marchant*:[157]

> [13] [T]he section sets out a series of steps which must be taken when it transpires that a director has a personal interest in a matter from which the directors must make a decision. The section requires the affected director to disclose the interest and its general nature before the matter is considered at a meeting, and to disclose to the meeting any material information relating to the matter which is known to the director. He may disclose what are called "observations of pertinent insight" relating to the matter if requested to do so. But the director

---

151. Cook v. Deeks 1916 (1) AC 554 (PC) (Can.); *African Claim and Land Co. v. WJ Langermann* 1905 TS 494 at 523.

152. Companies Act 71 of 2008 § 163; *see infra* Section V.A.

153. 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 213-14.

154. *Id.*

155. *Id.*

156. Companies Act 71 of 2008 § 75.

157. *Kensal Rise Invs. (PTY) Ltd. v. Marchant* [2014] [1523/2013 [2014] ZAKZDAC47 (30 October 2014) para. 13] (S. Afr.).

> may take no part in the decision-making process. Section 75(7) is then to the effect that a decision of the board, or a transaction or agreement approved by the board will be valid despite any personal financial interest of the director only if it was approved following disclosure of that interest in a manner required by the section; or, when there was no such disclosure, if it is subsequently ratified by an ordinary resolution of shareholders following the disclosure of that interest; or if the court declares it valid. It seems to me that the section endorses the common law position, and perhaps carries it a little further by rendering formalities mandatory.[158]

B. The Directors' Duty of Skill and Care

South African common law concerning a director's duties of skill and care also follows the English law. It has been summarized in *Fisheries Development Corp. of SA Ltd. v. Jorgensen & Another* [159] as follows:

> To determine whether there was negligence in any of the conduct alleged, it is necessary to have regard to the relevant aspects of a director's duty of care and skill. In England, certain principles have emerged from decided cases on that duty. There has been a relative paucity of cases in South Africa, but the essential principles of this branch of company law are the same, and the English cases provide valuable guidance . . . . The extent of a director's duty of care and skill depends to a considerable degree on the nature of the company's business and on any particular obligations assumed by or assigned to him . . . . In that regard, there is a difference between the so-called full-time or executive director, who participates in the day-to-day management of the company's affairs or a portion thereof, and the non-executive director who has not undertaken any special obligation. The latter is not bound to give continuous attention to the affairs of the company. His duties are of an intermittent nature to be performed at periodical board meetings, and at any other meetings which may require his attention. He is not, however, bound to attend all such meetings, though he ought to whenever he is reasonably able to do so . . . . Of course if he has reasonable grounds for believing such to be necessary, he ought to call for further meetings. 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 . . . . He is nevertheless expected to exercise the care which can reasonably

158. *Id.*

159. *Fisheries Development Corp. of SA Ltd. v. Jorgensen & Another Fisheries Dev. Corp. of SA Ltd. v. AWJ Invs. (PTY) Ltd. & Others* 1980 (4) SA 156 (W) at 165 F-166 E.

> be expected of a person with his knowledge and experience . . . . A director is not liable for errors of judgment . . . . In respect of all duties that may properly be left to some other official, a director is, in the absence of grounds of suspicion, justified in trusting that official to perform such duties honestly. He is entitled to accept and rely on the judgment, information and advice of the management, unless there are proper reasons for querying such. Similarly, he is not bound to examine the company's books . . . . Obviously, a director exercising reasonable care would not accept information and advice blindly. He would accept it, and he would be entitled to rely on it, but he would give it due consideration and exercise his own judgment in the light thereof. *Gower* . . . refers to the striking contrast between the directors' heavy duties of loyalty and good faith and their very light obligations of skill and diligence. Nevertheless, a director may not be indifferent or a mere dummy. Nor may he shelter behind culpable ignorance or failure to understand the company's affairs.[160]

C. Standards of Directors' Conduct Under the New Companies Act

At first blush, section 76 of the New Companies Act appears to be an attempt to codify the common-law with regard to directors' standards of conduct.[161] However, it has been held it is not a codification of a director's common law fiduciary duty, but simply a clarification.[162] In terms of section 76(2) of the New Companies Act, a director must—

(a) not use the position of the director, or any information obtained while acting in the capacity of a director—
    (i) to gain an advantage for the director or any other person other than the company or a wholly-owned subsidiary of the company; or
    (ii) to knowingly cause harm to the company or a subsidiary of the company; and
(b) communicate to the board at the earliest practicable opportunity any information that comes to the director's attention, unless the director—
    (i) reasonably believes that information is—
        (aa) immaterial to the company; or
        (bb) generally available to the public, or known to other directors; or

---

160. *Id.*

161. *Kensal Rise Invs. (PTY) Ltd.* 1523/2013 [2014] ZAKZDAC47 (30 October 2014) at paras. 11-12 (S. Afr.); *Sanlam Capital Mkts. (Pty) Ltd. v. Mettle Manco (Pty) Ltd. & Others* 2014 3 All SA 453 (GJ).

162. *Kensal Rise Invs. (PTY) Ltd.* [2014] ZAKZDAC47 (30 October 2014) at paras. 11-12 (S. Afr.); *Sanlam Capital Mkts. (Pty) Ltd.* [2014] 3 All SA 453 (GJ).

> (ii) is bound not to disclose that information by a legal or ethical obligation of confidentiality.[163]

It is apparent that section 76(2) is little more than clarification and formalization of the common-law position as stated in *Robinson v. Randfontein Estate Gold Mines*.[164]

Section 76(3) of the New Companies Act provides:

> (3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of a director—
>
> (a) in good faith and for a proper purpose;
>
> (b) in the best interest of the company; and
>
> (c) with a 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.[165]

At common law a director was required only to exercise the standards of skill and care which could "reasonably be expected of a person with his knowledge and experience."[166] However, section 76(3) also requires the director to meet an objective standard—that of the degree of care, skill, and diligence that can reasonably be expected of a person carrying out the same functions in relation to the company as those carried out by that director.[167] This is a significant advance on the common law position which previously indulged relatively ill-educated directors. It is clear from the section that it is inappropriate to take on an appointment as a director if one does not have sufficient education and knowledge to discharge one's obligations with a reasonable degree of skill and care. The requirement that the directors must act "*in good faith and for a proper purpose*" is essentially a reiteration of the common law.[168] The

---

163. Companies Act 71 of 2008 § 76(2).

164. *Robinson v. Randfontein Estates Gold Mining Co.* 1921 AD 168 at 177-80.

165. Companies Act 71 of 2008 § 76(3).

166. *Fisheries Dev. Corp. of SA Ltd. v. Jorgensen & Another Fisheries Dev. Corp. of SA Ltd. v. AWJ Invs. (PTY) Ltd. & Others* 1980 (4) SA 156 (W) at 165 F.

167. *Compare id.*, *with* the New Jersey decision of Francis v. United Jersey Bank, 432 A.2D 814 (N.J. 1981) (holding that a widow who was a director liable for damages where her fault lay in inattention while her two sons (who were also majority shareholders in the company) looted the company).

168. *Rex v. Milne & Erleigh* 1951 (1) SA 791 (A) at 828-30; EDGAR S. HENOCHSBERG, HENOCHSBERG ON THE COMPANIES ACT 297 (D.B. Friedman & P.M. Meskin eds., 2d ed. 1963).

same duties are also owed at common law to the company by nonexecutive directors.[169]

Section 76(4) introduces into South African law the "*business judgment rule*," which has a history in American law going back 170 years.[170] In *Miller v. American Telephone & Telegraph Co.*,[171] the U.S. Court of Appeals for the Third Circuit summarized the American rule as follows:

> The sound business judgment rule . . . expresses the unanimous decision of American courts to eschew intervention in corporate decision-making if the judgment of directors and officers is uninfluenced by personal considerations and is exercised in good faith . . . . Underlying the rule is the assumption that reasonable diligence has been used in reaching the decision which the rule is invoked to justify.[172]

Gevurtz[173] states in connection with the business judgment rule, as applied by American courts that:

> So far, in looking at cases in which the complaint is that the directors were not paying attention, we have seen courts generally apply the reasonably prudent person's test in a manner familiar to students of tort law. Things change when the complaint is not that the directors were inattentive but, rather, that the directors made a business decision for the corporation which turned out poorly, or which the plaintiff asserts was otherwise a poor decision.[174]

The New Companies Act attempts to define the business judgment rule, as it applies in South Africa, as follows:

> 76(4) 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 the company—
>
> (a) will have satisfied the obligations of subsection (3)(b) and (c) if—
>
> (i) the director has taken reasonably diligent steps to become informed about the matter;
>
> (ii) either—
>
> (aa) the director had no material personal financial interest in the subject matter of the decision, and

---

169. *Howard v. Harrigel & Another NNO* 1991 (2) SA 660 (A) at 678.

170. Percy v. Millaudon, 8 Mart. (n.s.) 68, 78 (La. 1829); FRANKLIN A. GERVURTZ, CORPORATION LAW 287 (2d ed. 2000); HENOCHSBERG, *supra* note 168, at 297.

171. Miller v. Am. Tel. & Tel. Co., 507 F.2d 759, 762 (3d Cir. 1974).

172. *Id.*

173. GERVURTZ, *supra* note 170, at 34.

174. *Id.*

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[175] with respect to any interest contemplated in subparagraph (aa); and

(iii) the director made a decision, or supported the decision of a committee of 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; and

(b) is entitled to rely on—

(i) the performance by any of the persons—

(aa) referred to in subsection (5); or

(bb) 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; and

(ii) any information, opinions, recommendations, reports or statements, including financial statements and other financial data, prepared or presented by any of the persons specified in subsection (5).

(5) To the extent contemplated in subsection (4)(b), a director is entitled to rely on—

(a) one or more 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;

(b) 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—

(i) within the particular person's professional expert competence; or

(ii) as to which the particular person merits confidence; or

(c) a committee of the board of which the director is not a member, unless the director has a reason to believe that the actions of the committee do not merit confidence.[176]

175. In other words, the director made the required disclosures to the board.

176. Companies Act 71 of 2008 § 76(4)-(5).

The difficulty with the formulation of the business judgment rule in sections 76(4) and 76(5) is that it may have the effect of watering down a director's obligation to act with the requisite degree of care, skill, and diligence. The sections simply require that the director takes reasonably diligent steps to become informed about the matter and that he or she has a rational basis for believing that the decision is in the best interests of the company.[177] However, it does not follow that, by taking reasonably diligent steps to become informed about the matter, the director acts with the requisite degree of care, skill, and diligence required of a person performing his functions or with his level of skill in evaluating the information.[178] It effectively characterizes negligence as the failure to be reasonably informed rather than the failure to take due care in the broad sense of the word.[179] Insofar as the director is entitled to rely on information obtained from employees of the company and the company's professional advisors, the requirement appears to be on all fours with the common law.[180]

D. To Whom Does the Director Owe a Fiduciary Duty and a Duty of Skill and Care?

A director owes a duty of care only to the company, not to: (1) the shareholders individually; (2) the company's creditors; (3) generally speaking to its subsidiaries; or, (4) where the company is a group of companies, to the group as a whole.[181] The principle that shareholders owe a duty of care only to the company derives from the English case of *Percival v. Wright*.[182] Unfortunately, the decision of the court in this case is somewhat perfunctory and probably out of date in certain respects.

In *Percival v. Wright*, the directors of a company purchased shares from other shareholders without disclosing that a third party had made an

---

177. *See id.*

178. *See id.*

179. *See id.*

180. *Fisheries Dev. Corp. of SA Ltd. v. Jorgensen & Another Fisheries Dev. Corp. of SA Ltd. v. AWJ Invs. (PTY) Ltd. & Others* 1980 (4) SA 156 (W) at 165.

181. *Kuwait Asia Bank EC v. Nat'l Mutual Life Nominees Ltd.* 1991 (1) AC 187 at 217-18; *Sage Holdings Ltd. v. The Unisec Group Ltd. & Others* 1982 (1) SA 337 (W) at 365 A; *Lipschitz v. Landmark Consol. (Pty) Ltd.* 1979 (2) SA 482 (W) at 488; *Rex v. Milne & Erleigh* 1951 (1) SA 791 (A) at 827; *Bell v. Lever Bros. Ltd.* 1932 AC 161 at 228; Percival v. Wright (1902) 2 Ch 421 (Eng.); *In Re* Wincham Shipbuilding, Boiler & Salt Co. (1878) 9 Ch 322 (CA) 328-29 (Eng.); Pergamon Press Ltd. v. Maxwell 1970 (2) All ER 809 (Eng.); Scottish Coop. Wholesales Soc'y Ltd. v. Meyer 1958 (3) All ER 66 (HL) 87-88 (Eng.); 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 132.

182. *Percival* (1902) 2 Ch 421 (Eng.).

offer to purchase the assets of the company at an advantageous price.[183] The court rejected the plaintiff's lawsuit on the basis that the directors were not trustees for the individual shareholders and that they could, therefore, buy their shares without disclosing pending negotiations for the sale of the company's undertaking.[184] While the principle that the directors do not, in general, owe a fiduciary duty to the individual shareholders has not been seriously questioned in England or South Africa, its application in the context of the facts that arose in *Percival v. Wright* has been seriously questioned.[185] Having regard to modern concepts of fair play between directors and shareholders, including the unlawfulness of insider trading, South Africa, Australia, New Zealand, and England have questioned whether the broad principle enunciated in *Percival v. Wright* can stand (i.e., that a director who is engaged in buying and selling shares to a shareholder has no duty to disclose inside knowledge that the director may have concerning the potential value of his shares).[186]

In the South African context, the *Percival v. Wright* principle was analyzed in *Sage Holdings Ltd. v. The Unisec Group Ltd. & Others* 1982 (1) SA 337 (W) 365A. There the court stated:

> Counsel for the respondents stressed that directors of a company owe a fiduciary duty to their company only and not to the individual shareholders of the company. He relied for that proposition upon *Percival v. Wright* (1902) 2 Ch 421. In that case directors purchased shares from the members of the company without revealing that negotiations were in progress for a sale of the undertaking at a favourable price. Gower . . . refers to 'his much-criticised decision.' At 574 he notes: 'The *Percival v. Wright* rule was severely criticised by the Cohen Committee, and forthrightly rejected by the Jenkins Committee in one of their bolder moods.' It is relevant in this context that, in s233 of the Act, the Legislature, for the first time has made "insider trading" a criminal offence. No person, including a director, who has knowledge of any information concerning a transaction or proposed transaction, or the affairs of a company which is expected to affect the price of such shares if publicly known, may deal in such shares to his direct or indirect advantage, prior to public announcement of such information . . . . It is also pointed out in Cilliers, Benade & De Villiers in *Company Law* 3rd ed at 264 that:

183. *Id.* at 422-23.
184. *Id.* at 426.
185. *See Sage Holdings Ltd. v. The Unisec Group Ltd & Others* 1982 (1) SA 337 (W) at 385 A.
186. *See id.*

> 'Whatever the interpretation placed on [*Percival v. Wright*] in England, the judgment ought not to be interpreted so widely by a South African Court as to absolve directors from all responsibility towards a buyer or seller of the shares of their company.'[187]

In *Coleman & Others v. Myers & Others*, the New Zealand Court of Appeal considered *Percival v. Wright*.[188] In the trial court, Justice Mahon expressed the view that *Percival v. Wright* was wrongly decided and stated the following:

> In the present case, which is the case of a private company with unlisted shares, it seems an untenable argument to suggest that the shareholders on an offer to buy their shares are not perforce constrained to repose a special confidence in the directors that they will not be persuaded into a disadvantageous contract by non-disclosure of material facts. In my opinion, therefore, there is inherent in the process of negotiation for sale a fiduciary duty owing by the director to disclose to the purchaser any fact, of which he knows the shareholder to be ignorant, which might reasonably and objectively control or influence the judgment of the shareholder informing his decision in relation to the offer. The application of the rule so assumed to exist must necessarily be confined to private companies and to such transactions in public company shares, listed or otherwise, where the identity of the shareholder is known to the director at the time of the sale.[189]

In Re Chez Nico (Restaurant) Ltd., the English Chancery Division followed *Coleman v. Myers* and held that the proposition in *Percival v. Wright* had been too widely interpreted, based only upon the headnote.[190] The text of the entire case did not support the general proposition set out in the headnote.[191] The court held:

> The only decision was that in general the fiduciary duties of directors are owed to the company, not to the shareholders, and that on the concessions made there was nothing in the facts of that case to justify imposing any duty on the directors to the shareholders as opposed to the company. The actual decision does not bear out the headnote. Like the Court of Appeal in New Zealand, I consider the law to be that in general directors do not owe fiduciary duties to shareholders but owe them to the company, however, in certain special circumstances fiduciary duties, carrying with them a duty of

187. *Id.* at 365-66.
188. *Coleman & Others v. Myers & Others* 1977 (2) NZLR 225 (NZCA) (N.Z.).
189. *Id.*
190. *In Re* Chez Nico (Restaurant) Ltd. 1992 BCLC 192 at 208.
191. *See id.*

> disclosure, which place directors in a fiduciary capacity vis-à-vis the shareholders.[192]

In *Glandon (Pty) Ltd. & Others v. Strata Consolidated (Pty) Ltd.*, Justice Mahoney held in the Supreme Court of New South Wales, Australia, that:

> The relationship of director and shareholder, as such and without more, does not give rise to a fiduciary relationship between the director and the shareholder. However, in some circumstances a fiduciary relationship may exist between a director purchasing a shareholder's shares and the shareholder. While the principle laid down in *Percival v Wright* stands, the factual and legislative context in which that principle is now to be applied is significantly different to when it was first established.[193]

If one accepts that *Percival v. Wright* does not prevent shareholders from claiming against a director who bought from or sold shares to them, where the director breaches a duty at common law, the problem that arises from *Percival v. Wright* can be addressed by an application of the South African common law of contract or tort.[194]

In *ABSA Bank Ltd. v. Fouche*,[195] the South African Supreme Court of Appeal considered the obligation of a party to a contract to make disclosure of certain facts before the contract was concluded.[196] The Court held:

> The policy considerations appertaining to the unlawfulness of a failure to speak in a contractual context—a non-disclosure—have been synthesised into a general test for liability. The test takes account of the fact that it is not the norm that one contracting party need tell the other all he knows about anything that may be material . . . . That accords with the general rule that where a conduct takes the form of an omission, such conduct is *prima facie* lawful . . . . A party is expected to speak when the information he has to impart falls within the exclusive knowledge (so that in a practical business sense the other party has him as his only source) and the information, moreover, is such that the right to have it communicated to him "would be mutually recognised by honest men in the circumstances.[197]

---

192. *Id.*

193. *Glandon (Pty) Ltd. & Others v. Strata Consol. (Pty) Ltd.* 1993 11 ACSR 453 (NSWCA) at 11-12, 15 (Austl.).

194. *See Gihwala v. Grancy Prop. Ltd.* 2017 (2) SA 337 (SCA) at paras. 107-10 (holding that a shareholder can maintain a separate cause of action against a director for breach of a legal duty undertaken by the director to the shareholder in an agreement that is separate and independent from the obligations of the director to the company for breach of fiduciary duty).

195. *ABSA Bank Ltd v. Fouche* 2003 (1) SA 176 (SCA) at 180-81.

196. *Id.*

197. *Id.*

In *McCann v. Goodall Group Operations (Pty) Ltd.*,[198] the South African court held:

> From the aforegoing exposition of the law the following principles emerge:
>
> . . . .
>
> (c) A negligent misrepresentation by way of an omission may occur in the form of a non-disclosure where there is a legal duty on the defendant to disclose some or other material fact to the plaintiff and he fails to do so.
>
> (d) Silence or inaction as such cannot constitute a misrepresentation of any kind unless there is a duty to speak or act as aforesaid.
>
> Examples of a duty of this nature include the following:
>
> (i) A duty to disclose a material fact when the fact in question falls within the exclusive knowledge of the defendant and the plaintiff relies on the frank disclosure thereof in accordance with the legal convictions of the community.
>
> (ii) Such duty likewise arises if the defendant has knowledge of certain unusual characteristics relating to or circumstances surrounding the transaction in question and policy considerations require that the plaintiff be apprised thereof.[199]

In *Dibley v. Furter*,[200] the defendant sold property to the plaintiff without disclosing to him that the property had been used as a graveyard.[201] Evidence led to the conclusion that a purchaser with knowledge of the graveyard would have offered less for the property.[202] The court held:

> I am of the opinion that the defendant knew that the presence of the graves on the property was a circumstance, attaching to the property, of a very peculiar nature such as one would not normally expect to find on a property of that kind. I am also satisfied that the defendant knew that if this fact were made known to prospective buyers they might not wish to buy. And I am satisfied the defendant knew that the plaintiff did not know, nor had any reason to suspect, that portion of the property had been used as graveyard. I am also satisfied that at the time of the sale the defendant did not inform the plaintiff of the graves because he thought that if the plaintiff knew he might not buy. Due to the peculiar nature of the defect in the property the defendant, in my opinion, knew that the plaintiff might be labouring under a misconception as to the true nature of the thing he was

198. *McCann v. Goodall Grp. Operations (Pty) Ltd.* 1995 (2) SA 718 (C) at 726 B.
199. *Id.*
200. *Id.*; *Dibley v. Furter* 1951 (4) SA 73 (C) at 89.
201. *Dibley* 1951 (4) SA 73 (C) at 89.
202. *Id.*

> buying and he did not inform him because he thought that if he did the plaintiff might no longer want to buy.[203]

In that case, the court ordered that the defendant refund the purchase price to the plaintiff.[204] In addition, the plaintiff was awarded damages to compensate him for the cost of engaging in the transaction.[205]

Accordingly, in the situation that arose in *Percival v. Wright*, a modern South African court would probably conclude that the pending offer to purchase the assets of the company was within the exclusive knowledge of the director/purchasers; that the plaintiffs had no way of knowing that there was such an offer pending; that the directors knew that the plaintiffs had no knowledge that there was such an offering pending; and that had the plaintiffs known the offer was pending they would not have sold at that particular price.[206] Under these circumstances, in the modern South African context, the plaintiffs/sellers would probably have been able to avoid the contract or claim damages without having to demonstrate that the directors had a fiduciary duty to them in general.[207] By purchasing shares in their personal capacity, the directors entered into a direct relationship with the shareholder which should have given rise to an independent source of liability that did not depend on its legal efficacy upon an underlying fiduciary duty.[208]

E. Remedies Available to the Company When the Director Breaches His Obligations to the Corporation

Section 77(2) expressly provides that a director may be held 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 section 75, 76(2) or 76(3)(a) or (b) of the Companies Act.[209]

What the legislature appears to have intended was that principles of common law should apply in relation to the manner of computation of damages and a director's obligation to restore secret profits. The manner of calculating damages in tort under South African law has been set out in Part II above. The effect of section 77(2) is, therefore, that a potential

---

203. *Id.*
204. *Id.*
205. *Id.*
206. *Id.*; Percival v. Wright (1902) 2 Ch 421 (Eng.).
207. *Percival* (1902) 2 Ch 421 (Eng.); *Dibley* 1951 (4) SA 73 (C) at 89.
208. *Percival* (1902) 2 Ch 421 (Eng.); *Dibley* 1951 (4) SA 73 (C) at 89.
209. Companies Act 71 of 2008 § 77(2)

award of damages against a director for breach of duty as set out in sections 75, 76(2) and 76(3) remains finite in the sense that the damage has to be proved on a sum formula basis.[210]

In addition to common law tort remedies, the company has other remedies against a director or an entity related to the director that has made an unlawful secret profit at the company's expense.[211] These remedies were summarized in *Robinson v. Randfontein Estate Gold Mining Co. Ltd.*[212] as follows:

> Now the question of the remedies available against a director who, without due disclosure, disposes of his own property to his company has been dealt with in a number of comparatively recent English decisions, the high authority of which renders unnecessary the consideration of earlier cases. See *Erlanger v New Sombrero Company* (3 A.C. p. 1218); *Carendish-Bentinck v Fenn* (12 A.C. p. 652); *Burland v Earle* (1902, A.C. p. 83); *Cook v Deeks* (1916, A.C. 1 p. 554, etc). And it is clear from these decisions that, in every enquiry, regard must be had to the relationship in which the director stood to the company when he acquired the property. The test is not what honor would dictate, but what the law will allow and that depends upon his duty to the company at the date of acquisition. If he was under an obligation at the time to acquire the property for the company, instead of for himself, then his non-disclosure will entitle it to repudiate the sale and restore the original position, because, as already explained, the transaction could not bind the company without its free consent. It could affirm the contract, but only by an acquiescence in its terms. The acquisition being untainted by any breach of duty, the company's only claim to the subject matter would be based on the contract. It could not seek to retain the property at a price reduced by a deduction of the director's profit. For that would amount to a new contract between the parties. When, however, the director's default extends further than non-disclosure, when a breach of duty attended the original acquisition, then the company may, if it chooses, retain the property purchased and also demand a refund of the profits. The ground upon which this relief is given is variously expressed. Profits may be claimed, it is said, when the property was acquired under circumstances which constituted the director a trustee of the company, or which conferred the equitable ownership upon the company, or when the director stood at the time in a fiduciary relationship towards the company,—by which I understand a fiduciary relationship directly affecting the acquisition. The test is expressed, for the most part, in terms peculiar to the English law; but the principle which underlies it is not

210. *Id.* at §§ 75; 76(2)-(3); 77(2).
211. *Robinson v. Randfontein Estate Gold Mining Co. Ltd.* 1921 AD 168 at 177-80.
212. *Id.*

> foreign to our own. For it rests upon the broad doctrine that a man who stands in a positon of trust towards another cannot, in matters affected by the position, advance his own interests (e.g., by making a profit) at the other's expense.[213]

This was further elaborated upon in *Phillips v. Fieldstone Africa (Pty) Ltd. & Another*,[214] where the court held:

> [30] The principles which govern the actions of a person who occupies a position of trust towards another were adopted in South Africa from the equitable remedy of English law. The Roman and Roman-Dutch law provided equivalent relief. In *Transvaal Cold Storage Co Ltd v Palmer* 1904 TS 4 at 19-20 and 34-5 the sources were considered and the conclusion was expressed that the extension and refinement of the Civil Law by English courts was a development of sound doctrine suited to 'modern conditions'. The fullest exposition in our law remains that of Innes CJ in *Robinson v Randfontein Estates Gold Mining Co Ltd* (*supra*) at 177-180 . . .[215]
>
> The principles so stated remain true, not only for this country, but also in many Commonwealth (and United States) jurisdictions.[216]
>
> [31] The following short summary attempts to encapsulate the present level of development. The rule is a strict one which allows little room for exceptions . . . . It extends not only to actual conflicts of interest but also to those which are a real sensible possibility . . . . The defences open to a fiduciary who breaches his trust are very limited: only the free consent of the principal after full disclosure will suffice . . . . Because the fiduciary who acquires for himself is deemed to have acquired for the trust . . . once proof of a breach of fiduciary duty is adduced it is of no relevance that (1) the trust has suffered no loss or damage . . . (2) the trust could not itself have made use of the information, opportunity etc. . . . or probably would not have done so . . . (3) the trust, although it may have used the information, opportunity etc. has refused it or would do so . . . (4) there is no privity between the principal and the party with whom the agent or servant is employed to contract business and the money would not have gone into the principal's hands in the first instance . . . or (6) the fiduciary acted honestly and reasonably . . . (although English and Australian courts make some allowance for equity in calculating the

---

213. *Id.* at 178-79.

214. *Phillips v. Fieldstone Africa (Pty) Ltd. & Another* 2004 (3) SA 465 (SCA).

215. *See Robinson* 1928 AD 168, at 177-80.

216. In connection with the United States, *compare* 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 130-35, *with* GERVURTZ, *supra* note, at 170.

> scope of the disgorgement in such cases). The duty may extend beyond the term of the employment.[217]

The statement that it is irrelevant whether "the trust has suffered no loss or damage" does not mean that damages can be claimed without proof according to a sum formula approach.[218] It simply means that the transaction can be avoided or the secret profit claimed, regardless of whether the company has suffered loss.

It follows that, where there has been a failure to make disclosure, the company can avoid the transaction, no matter how fair it may be provided that it makes *restitutio in integrum* (i.e., restore what it has obtained under the contract). The company may seek to recover any profits that the director has made as a result of the contract as well as any damages that the company has suffered as a result of the director's nondisclosure.[219] Alternatively, the company can elect to affirm the transaction, in which case the company can still claim any secret profit that it can prove from the delinquent director. There is no right to claim punitive or exemplary damages.

Disgorgement of the director's secret profit is a more elastic concept than proving damages on a sum formula approach because it may involve transferring to the company an asset that was acquired in breach of the rule after the court has set the transaction aside.[220] However, this is ameliorated by the fact that a monetary claim for the payment of secret profits is a damages claim that must be calculated on a sum formula approach that would have to be reduced by any appreciation in the property that occurred after the illegal transaction but before the restoration to the company.[221]

South African law does not recognize the English concept of a constructive trust that "obliges the trustee to account to the equitable owner."[222] This does not mean that South African law "provides no equivalent remedy. On the contrary, it has been observed that our law

---

217. *Phillips* 2004 (3) SA 465 (SCA) at 478-80.

218. *Id.*

219. 4 THE LAW OF SOUTH AFRICA, *supra* note 77, at 105.

220. *Da Silva v. CH Chemicals (Pty) Ltd.* 2008 (6) SA 620 (SCA) at para. 19; *Robinson v. Randfontein Estate Gold Mining Co.* 1921 AD 168 at 179-80, 200.

221. *Da Silva* 2008 (6) SA 620 (SCA) at paras. 56-58; *Phillips* 2004 (3) SA 465 (SCA) at paras. 27-33; *Atlas Organic Fertilizers (Pty) Ltd. v. Pikkewyn Ghwano (Pty) Ltd. & Others* 1981 (2) SA 173 (T) at para. 138 H; *Robinson v. Randfontein Estate Gold Mining Co.* 1921 AD 168 at 168.

222. *Kerbyn 178 (Pty) Ltd. v. Van Den Heever & Others NNO* 2000 (4) SA 804 (W) at 817 E.

has no need to receive the concept from English law precisely because it provides its own 'ample battery of remedies in personam' in similar circumstances."[223] For example, at common law, the Actio Pauliana[224] is available to the liquidator of an insolvent company to set aside an alienation that took place in fraud of creditors.

In *Fedsure Life Assurance v. Worldwide Africa Investment Holdings (Pty) Ltd. & Others*,[225] the court recognized that a shareholder suing derivatively, could obtain an injunction to prevent the disposition of a fund of money that had been misappropriated by the directors from the company.[226] In delivering its judgment, the court held:

> [29] Money, like any species of property, may be interdicted[227] pending a vindicatory[228] or quasi-vindicatory claim for that money. There is, however, a problem in this regard. As Schutz JA said in First National Bank of Southern Africa Ltd v Perry NO and Others 2001 (3) SA 960 (SCA) at 967H-I:
> 'It might seem a simple thing to recover stolen money from one found in possession of it. But the matter is complicated by the rule in our law, an inevitable rule it seems to me, flowing from physical reality, that, once money is mixed with other money without the owner's consent, ownership in it passes by operation of law . . . .'
> [30] If the money to be interdicted is identifiable with or earmarked as a particular fund to which the plaintiff claims to be entitled, the money may be interdicted . . . .
> [31] Money remains earmarked where the property of the applicant has been realised and the respondent is in possession of the proceeds, where the proceeds are clearly identifiable.[229]

---

223. *Id.* at 817 E-F; *Bodwditch v. Peel & Magill* 1921 AD 561 at 572-73 ("A person who has been induced to contract by the material and fraudulent misrepresentation of the other party may either stand by the contract or claim rescission"); RICHARD HUNTER CHRISTIE & G.B. BRADFIELD, THE LAW OF CONTRACT IN SOUTH AFRICA 297-304 (6th ed. 2016).

224. *Kerbyn* (4) SA 804 (W) at 817.

225. *Fedsure Life Assurance v. Worldwide Africa Inv. Holdings (Pty) Ltd. & Others* 2003 (3) SA 268 (W).

226. *Fedsure Life Assurance* 2003 (3) SA 268 (W) at 278-79.

227. Restrained or enjoined. *Interdicted*, BLACK'S LAW DICTIONARY (10th ed. 2014).

228. The court is here referring to the *rei vindicatio*, a common law cause of action that permits an owner who has been deprived of possession of his property to "vindicate" or pursue his property (referred to in Latin as the *res*) from whomever may be holding it (*see Chetty v. Naidoo* 1974 (3) SA 13 (A) at 20B (holding that the owner, in instituting a *rei vindicatio*, need, therefore, do no more than allege and prove that he is the owner and the defendant is holding the *res*—the onus being on the defendant to allege and establish a new right to continue to hold against the owner")). *Rei vindicatio*, BLACK'S LAW DICTIONARY (10th ed. 2014).

229. *First National Bank of Southern Africa Ltd v. Perry NO & Others* 2001 (3) SA 960 (SCA) at 967 H-I.

Even where misappropriated money is not clearly identifiable in the sense that it has been comingled with other money, the court will assume, in the absence of evidence to the contrary, that the misappropriated money remains in the bank account of the thief into which it was deposited.[230]

F. The Derivative Action

The rule that the fiduciary duties of a director are owed only to the company has the consequence that, save in exceptional circumstances, only the company can sue the directors for breach of that fiduciary duty.[231] This is known in England and South Africa as the *"rule in Foss v. Harbottle."*[232] In essence, the rule in *Foss v. Harbottle* prevents the individual shareholders of the company from asserting the company's claim against third parties where the company has a claim against the third party even in delict or in contract, save in exceptional circumstances.[233] The rule, which is central to our company law, recognizes that the company and the shareholders are separate entities.[234]

However, the rule in *Foss v. Harbottle* admits certain exceptions, most notably:

> When (1) the wrong complained of involves conduct which is either fraudulent or *ultra vires* and (2) the wrong has been perpetrated by directors or shareholders who are in the majority and so control the company.[235] In such circumstances the law recognises that an aggrieved minority shareholder has to have a remedy to enable him or her to recover on behalf of the company because the directors will not do so. Such an action is called a "derivative action."[236]

The nature and parameters of the common-law derivative action under South African law is, as noted above, derived from the English law commencing with *Foss v. Harbottle*.[237] It is also a concept that is recognized in the law of most American jurisdictions.[238]

---

230. *Fedsure Life Assurance v. Worldwide Africa Inv. Holdings (Pty) Ltd. & Others* 2003 (3) SA 268 (W) at paras. 34-45; *Lockie Bros. Ltd. v. Pezaro* 1918 WLD 60 at 61-62.

231. *See* Foss v. Harbottle (1843) 2 Hare 461 (67 ER 189) (Eng.).

232. *Id.*

233. *See id.*

234. *Golf Estates (Pty) Ltd. v. Malherbe & Others* 1997 (1) SA 873 (C) at 879.

235. *Francis Hill Family Tr. v. South African Reserve Bank* 1992 (3) SA 91 (A) at 97 B-D.

236. *Id.* at 97 C.

237. *Id.*

238. GERVURTZ, *supra* note 170, at 407.

In *Golf Estates (Pty) Ltd. v. Malherbe*,[239] the South African courts endorsed the following statement of principle by an English textbook writer, Gower:[240]

> Where such an action is allowed the member is not really suing on his own behalf nor on behalf of the members generally, but on behalf of the company itself. Although . . . he would have to frame his action as a representative one on behalf of himself and all the members other than the wrongdoers, this gives a misleading impression of what really occurs. The plaintiff shareholder is not acting as a representative of the other shareholders but as a representative of the company . . . . In the United States . . . this type of action has been given the distinctive name of a "derivative action," recognising that its true nature is that the individual member sues on behalf of the company to enforce rights *derived from it*.[241]

The common law derivative action has now been eliminated and replaced by section 165 of the New Companies Act, which provides for the pursuit of the remedy in a more specific and directed form.[242]

Section 165 of the New Companies Act provides:

> 165. Derivative actions.—
>
> (1) Any 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.
>
> (2) A person may serve a demand upon a company to commence or continue legal proceedings or take related steps, to protect the legal interests of the company if the person—
>
> (a) is a shareholder or a person entitled to be registered as a shareholder of the company or of a related company;
>
> . . . .
>
> (5) A person who has made a demand in terms of subsection (2) may apply to a court for leave to bring or continue proceedings in the name and on behalf of the company and the court may grant leave only if—
>
> (a) the company—
>
> (i) has failed to take any particular step required by subsection (4);
>
> . . . .

239. *Id.* at 879.

240. L.C.B. GOWER, GOWER'S PRINCIPLES OF MODERN COMPANY LAW 587 (5th ed. 1992).

241. *See also* Prudential Assurance Co. v. Newman Indus. Ltd. [1982] 1 All ER 354, 357j-358b (Eng.) (also an English case, which was approved in South Africa by the Supreme Court of Appeal in *Gihwala v. Grancy Prop. Ltd.* 2017 (2) SA 337 (SCA) at paras. 108-09).

242. Companies Act 71 of 2008 § 165.

> (v) has served a notice refusing to comply with the demand, as contemplated in subsection (4)(b)(ii); and
>
> (b) the court is satisfied that—
>
> (i) the applicant is acting in good faith;
>
> (ii) the proposed or continuing proceedings involve the trial of a serious question of material consequence to the company; and
>
> (iii) 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.[243]

In terms of section 165(15), a derivative action, once commenced, cannot be discontinued, compromised, or settled without the leave of the court.[244] The limited nature of the derivative action, and the fact that its parameters are clearly set out in the statute, also affords some protection to the majority shareholders and the directors and officers of the company when they have taken steps that a minority shareholder maintains are inappropriate.[245]

However, section 165 would not prevent an individual shareholder with an independent cause of action in tort against a director based upon a duty of care that does not arise out of a director's common law and statutory duty as a director from suing for damages.[246] In the case of a shareholder who bought or sold shares to a director who has inside knowledge that was not disclosed, the shareholder would arguably have an independent claim in tort arising out of an independent common law duty to disclose.[247] In addition, a director would not be protected by the operation of section 165 of the New Companies Act if the director's breach of fiduciary duty also involves the breach of a contractual obligation directly owing to an individual shareholder.[248] In *Gihwala v. Grancy Prop. Ltd*,[249] the SCA endorsed the following observations of the English judge Bingham LJ in *Gore Wood & Co. (a firm)*[250]:

---

243. *Id.*
244. *Id.* at § 165(15).
245. *Id.*
246. *Id.* at § 165.
247. *See* cases cited *supra* Section IV.D.
248. Companies Act 71 of 2008 § 165.
249. *Gihwala* 2017 (2) SA 337 (SCA) at para. 110.
250. Johnson v. Gore Wood & Co. [2001] 1 All ER 481 (HL) 503 f-g (Eng.).

> Where a company suffers loss caused by a breach of a duty to it, and a shareholder suffers loss separate and distinct from that suffered by the company caused by a breach of a duty independently owed to the shareholder, each may sue to recover the loss caused to it by breach of the duty owed to it but neither may recover loss caused to the other by breach of the duty owed to that other.[251]

G. Reckless Trading and the Directors' Potential Liability to Creditors and Shareholders

As noted above, section 424 of the Old Companies Act remains in full force and effect with regard to the winding-up of companies that are not *"solvent."*[252] This section creates potential liability for creditors and other officers of an insolvent company that has been carrying on business recklessly or fraudulently.[253] The South African law recognizes two forms of insolvency:

> factual insolvency (where a company's liabilities exceed its assets) and commercial insolvency (a position in which a company is in such a state of illiquidity that it is unable to pay its debts, even though its assets may exceed its liabilities).[254]

A company is "insolvent" (i.e., not solvent) within the meaning of section 9(1) of schedule 5 of the New Companies Act when it is "commercially insolvent"—i.e., unable to pay its debts as they become due.[255] Accordingly, section 424 of the Old Companies Act now applies only to fraudulent and reckless trading, where the company is also in winding-up and commercially insolvent, in the sense that it is unable to pay its debts as they become due.[256] This means that, where a company's liabilities exceed its assets (but it is able to pay its debts as they become due), section 424 does not apply.[257]

Section 424 of the Old Companies Act deals with the liability of directors and others for the fraudulent or reckless conduct of a company's business.[258] It provides that:

---

251. *Id.*
252. Companies Act 71 of 2008 sched. 5, § 9.
253. *Id.*
254. *Boschpoort Ondernemings (Pty) Ltd. v. ABSA Bank Ltd.* 2014 (2) SA 518 (SCA) at para. 16.
255. *Id.* at para. 22.
256. Companies Act 71 of 2008 sched. 5, § 9.
257. *Id.*
258. *Id.*

> When it appears . . . that any business of the company was or is being carried on recklessly or with the intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the court may, on the application of the Master,[259] the liquidator,[260] . . . any creditor or member or contributory of the company, declare that any person was knowingly a party to the carrying on of the business in the manner aforesaid, shall be personally responsible, without limitation of liability, for all or any of the debts or other liabilities of the company as the Court may direct.[261]

The effect of this section is that a director or other officer of an insolvent company may be sued by a creditor, a shareholder, or a liquidator appointed on insolvency, where he or she is a party to carrying on the business of the insolvent company fraudulently or recklessly.[262] This is an independent cause of action over and above any cause of action that may lie against a director who has breached his fiduciary duty, which, as noted above, is owed only to the company.[263] Before the enactment of the New Companies Act, the action could be brought by a creditor or member where all the other requisites were present, even where the company was still trading, was not insolvent, and had not been placed in liquidation.[264] However, as a result of the passage of the New Companies Act, the remedy is probably now only available where the company is in liquidation and insolvent.[265]

Insofar as the action can be brought by a member of the company, it may appear to be an exception to the rule that a shareholder can usually sue only derivatively.[266] However, the distinction is more apparent than real. The member's only right is to declare that the person who was knowingly a party to carrying on the business of the company recklessly or fraudulently is personally liable for the debts of the company.[267] Accordingly, unless the member is also a creditor, the action brought by the member would only benefit the member indirectly insofar as any

---

259. An official of the court who oversees South African winding-up (corporate bankruptcy) proceedings and performs a similar function to the U.S. trustee under 11 U.S.C. § 307 (1986).

260. The person charged with winding-up or liquidating an insolvent company, similar to a trustee appointed under Chapter 7 of the United States Bankruptcy Code.

261. Companies Act 71 of 2008 § 424.

262. *Id.*

263. *Id.*

264. *Body Corp. of Greenwood Scheme v. Seventy Five-Two Sandown (Pty) Ltd.* 1999 (3) SA 480 (W) at 487; *G. Bowman NO v. Sacks* 1986 (4) SA 459 (W) at 462 H.

265. Companies Act 71 of 2008 sched. 5, § 9.

266. *See Kalinko v. Nisbet & Other*s 2002 (5) SA 766 (W) at 777-78.

267. *Id.*

recovery under the section has the effect of restoring the insolvent company to solvency.[268]

As the claim can be made against "any person" who was a party to the carrying on of the business in the prohibited fashion, the claim can also be made against a juristic person, such as a company or a trust.[269] This means that a claim under this section can be made against a shareholder who is party to carrying on of the business in this manner.[270] The claim is available only against a person or entity who has been a party to the company's business in the sense that he "has joined with the company in a common pursuit. Generally, this would include its directors and managers, all of whom are acting in common pursuit of the company's business."[271] The section "does not extend to those who, while carrying on their own business, incidentally enable the company to carry on its business."[272] Accordingly, for example, an auditor who was merely carrying out his statutory functions and was not intentionally colluding with the company to enable it to trade recklessly or fraudulently will not be liable under the section.[273] Similarly, a broker who sells debentures in the insolvent company is not necessarily liable under the section.[274]

As a company can only act through human agency, it is necessary for a plaintiff suing a company under this section to demonstrate that the company, through its board or any of its directors, was aware that the defendant company was participating in the conduct of the business of another company recklessly or fraudulently.[275] This means that it must be proved that the person who is liable had knowledge of the facts from which a conclusion can properly be drawn that the business of the company was being carried on recklessly or with intent to defraud creditors of the company or for any fraudulent purpose.[276] It is not

---

268. *Id.*

269. *Cooper NNO v. SA Mutual Life Assurance Soc'y & Others* 2001 (1) SA 967 (SCA) at para. 16; *Anderson & Others v. Dickson & Another NNO* 1985 (1) SA 93 (N) at 110 A-B.

270. *Cooper NNO* 2001 (1) SA 967 (SCA) at para. 976 F-G.

271. *Id.* at para. 17; *Powertech, Indus.' Ltd. v. Mayberry & Another* 1996 (2) SA 742 (W) at 749 D-I.

272. *Cooper NNO* (1) SA 967 (SCA) at 976 I; *Powertech, Indus.' Ltd.* (2) SA 742 (W) at 749 D-I.

273. *Powertech, Indus.' Ltd.* SA 742 (W) at 750 I-751 A.

274. *Cooper NNO* (1) SA 967 (SCA) at 976-77 paras. 17-18.

275. *Id.* at 975-76 paras. 15-16; *Anderson & Others v. Dickson, & Another NNO* 1985 (1) SA 93 (N) at 109 I-110 B.

276. *Philotex (Pty) Ltd. v. Snyman* 1998 (2) SA 138 (SCA) at 143; *Ozinsky v. Lloyd* 1995 (2) SA 915 (A) at 917; *Howard v. Herrigel & Another NNO* 1991 (2) SA 660 (A) at 673-74.

necessary for the plaintiff to prove that the defendant also had actual knowledge of the legal consequences of those facts.[277]

The remedy is a punitive one.[278] The defendant can be held personally liable for the liabilities of the company without proof of any causal link between his conduct and these liabilities.[279] In this respect, this section goes further than the common law, which usually limits damages claims to damages that have a causal link to the breach of contract or tort.[280] A creditor must establish the amount of his claim.[281] However, where the applicant is a liquidator, it is not necessary that the court should state a particular amount for which the defendant should be held liable because a liquidator will not necessarily know who all of the company's creditors are at the time he brings the action.[282]

Fraud in this context involves a false representation made with "conscious deceit on the part of the person making" it which causes "actual or potential prejudice" to another.[283] It follows:

> The test is inevitably subjective. Unless the representor is shown to have been aware that his representation will tend to mislead, there is no element of conscious deceit and no fraud. The essential point is that the representor is aware that his representation will tend to mislead not only when he knows that it is false, but also when he knows that it may be false. In the latter case, no less than the former, he practices deceit if he misleads the representee into the belief that he (the representor) believes in the truth of the representation when he (the representor) can have no such honest belief, knowing that the representation may not be true.[284]

Being a party to the conduct of the business does not require that positive steps be taken.[285] It may be sufficient that the defendant merely concurs in the conduct of the business in that manner.[286]

---

277. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 143; *Herrigel & Another NNO* 1991 (2) SA 660 (A) at 673-74.

278. *Philotex (Pty) Ltd.* (2) SA 138 (SCA) at 142 G-I.

279. *Id.* at para. 142 G-I; *Herrigel* 1991 (2) SA 660 (A) at 672 E.

280. *Philotex (Pty) Ltd.* (2) SA 138 (SCA) at 142 G-I.

281. *Retail Mgmt. Servs. (Edms) Bpk v. Schwartz* 1992 (2) SA 22 (W) at 29-30; *Dorklerk Inv.' (Pty) Ltd. v. Bhyat* 1980 (1) SA 443 (W) at 447-48.

282. *Cronje v. Stone* 1985 (3) SA 597 (T) at 615 G; *Retail Mgmt. Servs. (Edms) Bpk* 1992 (2) SA 22 (W) at 29.

283. *Ex Parte Lebowa Dev. Corp. Ltd.* 1989 (3) SA 71 (T) at 101 D, 103 G.

284. *Id.* at 103 H.

285. *Philotex (Pty) Ltd. v. Snyman* 1998 (2) SA 138 (SCA) at para. 143 B-C; *Howard v. Herrigel & Another NNO* 1991 (2) SA 660 (A) at 674 H.

286. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at para. 143 B-C; *Howard* 1991 (2) SA 660 (A) at 674 H.

The test for recklessness is objective.[287] It includes gross negligence with or without consciousness of risk-taking.[288] It also includes an "entire failure to give consideration to the consequence of one's actions, in other words, an attitude of reckless disregard of such consequences."[289] It follows:

> The test for recklessness is objective insofar as the defendant's actions are measured against the standard of conduct of the notional reasonable person and it is subjective insofar as one has to postulate that notional being as belonging to the same group or class as the defendant, moving in the same spheres and having the same knowledge or means to knowledge.[290]

In other words, a director with significant qualifications and experience in finance and business could more easily be found to have been reckless than one with average skills.[291]

At first blush, there is very little difference between the requirements of fraud and of recklessness, especially because fraud can involve potentially making a representation that is not true with a reckless disregard as to its truth.[292] The matter is confused further by the fact that the courts may treat fraudulent conduct as reckless because that is an easier onus to satisfy.[293] For example, the courts have held that a misrepresentation by silence (i.e., a failure to disclose) by directors to the company's creditors that the company was in parlous financial straits constitutes reckless conduct.[294] However, that type of conduct is also arguably fraudulent.

While it is not absolutely essential to distinguish between fraud and recklessness in all cases, there is a fundamental difference that goes beyond intent. It is an essential element of fraud in South Africa that there be a false representation to the other party. Recklessness does not require that there be any representation at all.[295]

In *Philotex (Pty) Ltd.*, the court held the directors' recklessness included trading in a company that was "undercapitalised, terminally short of cash and possessed of a surplus of overvalued stock such as

---

287. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 143 G.
288. *Id.*
289. *Id.* at para. 143 F; *S v. Dhlamini* 1988 (2) SA 302 (A) at 308 D-E.
290. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 143 G-H.
291. *See id.*
292. *Ex Parte Lebowa Dev. Corp. Ltd.* 1989 (3) SA 71 (T) at 101 E-F.
293. *See id.*
294. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 186 D-E.
295. *Ex parte Lebowa* 1989 (3) SA 71 (T) 101D, 111C-I; *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 186A-D.

made a landslide of gross losses inevitable." There was no reasonable prospect of the company trading out of its difficulties.[296] The directors unreasonably risked trade creditors' money with a "wilful disregard of the consequences to trade creditors" and misrepresented the position to trade creditors through nondisclosure.[297]

It is not *per se* reckless or fraudulent to trade in insolvent circumstances.[298] However, once it becomes clear that the company will never be able to satisfy its creditors, a director who continues to trade will probably be guilty of both recklessness and fraud.[299] The conduct is fraudulent; because when a person incurs credit, he impliedly represents that the debtor believes he will be able to make payment of the debt when it falls due.[300]

The New Companies Act has inserted a provision to the effect that "a company must not carry on its business recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose."[301] "A director of a company is liable for any loss, damage or costs sustained by the company as a direct consequence of the director having . . . acquiesced in the carrying on of the company's business despite knowing that it was being conducted in a manner prohibited by section 22(1)."[302]

In terms of section 218(2) of the New Companies Act, any person who contravenes any provision of the Act is liable to *"any other person"* for any loss or damage suffered by that person as a result of that contravention. This means that a claim against a director who is a party to carrying on the business of the company fraudulently or recklessly can be made by any person, including the company, a shareholder, or a creditor.[303] In *Rabinowitz v. Van Graan*,[304] the court held that section 218(2) of the New Companies Act conferred a direct action by a shareholder against the directors where the business of the company had

---

296. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 186 D.

297. *Id.* at 186 A-D.

298. *Ex Parte De Villiers & Another NNO: In Re Carbon Developments (Pty) Ltd. (In Liquidation)* 1993 (1) SA 493 (A) at 504 B-C.

299. *Id.* at 503 C-504 C.

300. *Philotex (Pty) Ltd.* 1998 (2) SA 138 (SCA) at 503 H-J; *R v. Lamb* 1973 (3) SA 982 (A) at 984 G-H.

301. Companies Act 71 of 2008 § 22(1).

302. *Id.* § 77(3)(b).

303. *Sanlam Capital Mkts. (Pty) Ltd. v. Mettle Manco (Pty) Ltd.* [2014] 3 All SA 454 (GJ) at para. 41; *Rabinowitz v. Van Graan* 2013 (5) SA 315 (GSJ) at 320; HENOCHSBERG, *supra* note 168, at 639.

304. *Rabinowitz* 2013 (5) SA 315 (GSJ) at para. 19.

been conducted fraudulently or recklessly by the directors.[305] The court rejected an argument that this was effectively a derivative action and that the proper plaintiff was the company itself.[306]

However, a difficulty that a shareholder may face when making a claim under section 218 is proving its damages. The fact that the company has suffered loss as a result of the directors' fraudulent or reckless conduct does not necessarily mean that the shareholder suffered any loss at all.[307] The shareholder would have to prove the fraudulent or reckless conduct actually caused a diminution in the value of his shareholding.[308] One may ask whether it is necessary for the creditors or shareholders to have recourse to section 424 of the Old Companies Act in the light of the wide provisions creating liability under section 218 of the New Companies Act. The short answer is that when the claim relates to an insolvent company and, therefore, falls squarely within the ambit of section 424 of the Old Companies Act, it may be more advantageous to claim under that section for the following reasons.[309]

First, a claim under section 218(2) of the New Companies Act lies only against persons who specifically contravene a provision in the Act.[310] This will usually limit the claim to a claim against directors, whose conduct in trading recklessly amounts a breach of section 77 of the New Companies Act.[311] It would not apply to enable a claim against a shareholder or another person—not a director—who was a party to carrying on the business fraudulently or recklessly.

Second, a claimant under section 218 of the New Companies Act would have to prove that it has actually suffered damage, including the quantum of that damage and that there is a causal relationship between the delinquent conduct and the damage.[312] In other words, damages in a claim based upon section 218 of the New Companies Act would have to

---

305. *Id.*

306. *See also Gihwala v. Grancy Prop. Ltd.* 2017 (2) SA 337 (SCA) at paras. 107-10 (reasoning that the fact that the wrong may also have been done to a company does not prevent a shareholder from asserting an independent cause of action that the law allows him provided that he is not actually asserting the company's claim); *S. Africa Enter. Dev. Fund Inc. v. Indus. Credit Corp. Africa Ltd.* 2008 (6) SA 468 (W) at para. 16; George Fischer (Great Britain) Ltd. v. Multi Constr. Ltd. Dexion Ltd. (Third Party) [1995] 1 BCLC 260 (CA) 264e-267a (Eng.).

307. *See S. Africa Enter. Dev. Fund Inc.* 2008 (6) SA 468 (W) at para. 69.

308. *Id.*

309. Companies Act 71 of 2008 § 218.

310. *Id.* § 218(2).

311. *Id.* §§ 77, 218(2).

312. *Id.* § 218.

be proved and calculated on a sum formula basis.[313] In contrast, a claimant under section 424 of the Old Companies Act does not have to prove causation or actual damage.

V. SHAREHOLDER REMEDIES IN CASES OF OPPRESSIVE OR UNFAIRLY PREJUDICIAL CONDUCT

Where the conduct of the director or a company or its majority shareholder is unlawful and confers a cause of action upon the company, the shareholders can bring a derivative action.[314] However, where the conduct of the directors or the majority shareholders is not unlawful but is oppressive or unfairly prejudicial to the minority shareholder, South African law confers certain equitable remedies upon the minority shareholders who are unfairly prejudiced by the conduct of the majority.[315]

I have demonstrated in Part II above that South African courts are not courts of equity and are not generally empowered to apply equitable principles.[316] The conferment of equitable remedies upon a wronged minority shareholder is, therefore, a statutory exception to this general rule.[317] In broad terms, the alternative statutory equitable remedies available to an oppressed minority shareholder are (1) relief from oppression under section 163 of the New Companies Act, which could consist, among other things, in enjoining the conduct complained of, forcing the majority shareholders to buy out the minority shareholder, or appointing additional directors to the company's board in order to redress any imbalance; or (2) winding-up (or liquidating) the company.[318] These two remedies are analyzed below, along with certain others.

A. Relief from Oppressive or Unfairly Prejudicial Conduct (Section 163 of the New Companies Act)

Section 163 of the New Companies Act affords a wide equitable discretion to the court to redress oppressive or unfairly prejudicial

313. *Id.*
314. *Id.* § 165; sources cited *supra* Section III.E.
315. *See* Companies Act 71 of 2008 § 16.
316. *Brisley v. Drotsky* 2002 (4) SA 1 (SCA) at para. 9; *Weinierlien v. Goch Bldg. Ltd.* 1925 AD 282 at 295.
317. *Brisley* 2002 (4) SA 1 (SCA) at para. 9; *Weinierlien* 1925 AD 282 at 295.
318. Winding up is the South African equivalent of dissolution.

conduct.[319] That section is similar, although broader in its ambit, than section 252 of the Old Companies Act.[320] It follows:

> The old provision was directed at a particular act or omission of the company or the manner in which the affairs of the company were being conducted; the new provision includes acts or omissions of a related person or the manner in which the business of a related person is being conducted. The new provision also expressly includes the manner in which the powers of a director or prescribed officer are being or have been exercised.[321]

The two sections are sufficiently similar in that the courts have held that "there is a benefit to be derived from considering the jurisprudence developed over the years under prior acts as to what constitutes oppressive or unfairly prejudicial conduct."[322]

Section 163 of the New Companies Act confers a remedy on a shareholder or a director of a company.[323] Either the shareholder or the director may apply to a court for relief if:

> (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; or
> (c) 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.[324]

The court has wide powers to fashion a remedy. It may:

> make any interim or final order it considers fit, including an order restraining the conduct complained of; (d) an order to regulate the company's affairs by directing the company to amend its memorandum of incorporation or to create or amend a unanimous shareholder agreement; (e) an order directing an issue or exchange of shares; (f) an order appointing directors in place of or in addition to all or any of its directors

---

319. Companies Act 71 of 2008 § 163.

320. *Compare id.*, *with id.* § 252.

321. *Visser Sitrus (Pty) Ltd. v. Goede Hoop Sitrus (Pty) Ltd. & Others* 2014 (5) SA 179 (WCD) at para. 53.

322. *Grancy Prop. Ltd. v. Manala & Others* 2015 (3) SA 313 (SCA) at para. 22; *Visser Sitrus (Pty) Ltd.* 2014 (5) SA 179 (WCD).

323. Companies Act 71 of 2008 § 163.

324. *Id.*

> then in office; (g) an order directing the company or any other person to restore to a shareholder any part of the consideration that the shareholder paid for shares, or pay the equivalent value, with or without conditions; (h) an order varying or setting aside a transaction or an agreement to which the company is a party and compensating the company or any other party to that transaction or agreement; . . . (j) an order to pay compensation to an aggrieved person, subject to any other law entitling that person to compensation; or an order directing rectification[325] of the registers with other records of the company . . . .[326]

The powers of the court are not limited to those listed in section 163(2).[327]

Most commonly the aggrieved shareholder seeks to have his or her shares bought out.[328] In that event, difficulties arise in assessing a price because the value of the shares may have become depressed as a result of the unfair or prejudicial conduct of the majority shareholder.[329] In addition, because the minority shareholder is a minority shareholder, it would usually be unfair to order a buy out with a minority shareholder discount.

In *Blackman Jooste Everingham: Commentary on the Companies Act*, the authors, in analyzing section 252 of the Old Companies Act, state:

> The market price of the shares is not necessarily a fair price.[330] And where it is not, a valuation of the company's shares may be based on the company's ability to generate income (the company as a 'going concern');[331] or on the company's dividend stream (or its likely dividend

---

325. This is the Amendment of the share register to reflect a different shareholding.

326. Companies Act 71 of 2008 § 163(2).

327. *Grancy Prop. Ltd.* 2015 (3) SA 313 (SCA) at para. 29-32; *Bader & Another v. Weston & Another* 1967 (1) SA 134 (C) at 147 E.

328. Robert A. Rabbat, *Application of Share-Price Discounts and Their Role in Dictating Corporate Behavior: Encouraging Elected Buy-Outs Through Discount Application*, 43 WILLAMETTE L. REV. 107, 110 (2007).

329. *Id.* at 116.

330. *Benjamin v. Elysium Investments (Pty) Ltd.* 1960 (3) SA 467 (E); Re London School of Electronics Ltd. (1986) Ch 211 (Eng.); *Re Bagot Well Pastoral Co. (Pty) Ltd.* [1992] 9 ACSR 129, 146 SC (WA) (Austl.); *ES Gordon (Pty) Ltd. v. Idameneo No. 123 (Pty) Ltd.* (1994) 15 ACSR 536, 550-41 SC (NSW) (Austl.); Rankine v. Rankine 1995 18 ACSR 725 at 727-32 (Eng.); *Fixuto (Pty) Ltd. v. Bosnjak Holdings (Pty) Ltd. (No. 2)* (1998) 29 ACSR 290, 299 SC (NSW) (Austl.).

331. Re Abraham & Inter-Wide Inv. Ltd. [1985] 20 D.L.R. 4d 267, 277 (Can.); *Queensland Coop. Milling Ass'n Ltd. v. Hutchinson* (1976) 2 ACLR 188 SC at 42-43, para. 12 (Qld) (Austl.); Buckingham v. Francis (1986) 2 All ER 738, 738 (Eng.); Dean v. Prince 1954 Ch 409; [1954] 1 All ER 749 (CA) (Eng.).

> stream); or on what the company's assets would fetch if it were liquidated.[332]

South African law relating to oppressive conduct by a majority shareholder is heavily influenced by English law principles, which are familiar to Anglo-American lawyers.[333] In *Louw v. Nel*,[334] the court specifically approved the English decision of Lord Wilberforce in *Ebrahimi v. Westbourne Galleries Ltd. & Others* as follows:

> The foundation of it all lies in the words "just and equitable" and, if there is any respect in which some of the cases may be open to criticism it is that the courts may sometimes have been too timorous in giving them full force. The words are a recognition of the fact that a limited company is more than a mere judicial entity, with a personality in law of its own: there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se, which are not necessarily submerged in the company structure. This structure is defined by the Companies Act 1948 and by the articles of association by which shareholders agree to be bound. In most companies and in most contexts, this definition is sufficient and exhaustive, equally so whether the company is large or small. The "just and equitable" provision does not, as the respondent suggests, entitle one party to disregard the obligation he assumes by entering a company, nor the court to dispense him from it.[335] *It does, as equity always does, enable the court to subject the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way.*
>
> It would be impossible, and wholly undesirable, to define the circumstances in which these considerations may arise. Certainly the fact that a company is a small one, or a private company, is not enough. There are very many of these where the association is a purely commercial one, of which it can safely be said that the basis of association is adequate and exhaustively laid down in the articles.[336] The super-imposition of equitable

---

332. 2 BLACKMAN JOOSTE EVERINGHAM, COMMENTARY ON THE COMPANIES ACT 9-52 (2002).

333. *Louw & Others v. Nel* 2011 (2) SA 172 (SCA) at paras. 20-24 (referring, among things, to the seminal English law cases of Ebrahimi v Westbourne Galleries Limited & Others [1972] 2 All ER 492 at 500 a-h (Eng.) and O'Neill v Phillips [1999] 2 All ER 961 at 966) (Eng.); *Bayly v. Knowles* 2010 (4) SA 548 at para 23.

334. *Louw & Others* 2011 (2) SA 172 (SCA) at para. 21.

335. The court is here referring to the obligation a minority shareholder takes up when he acquires shares in the company and agrees to be bound by its constitution.

336. The company's constitution or, as it is referred to now in South Africa, the company's memorandum of incorporation.

> considerations requires something more, which typically may include one, or probably more, of the following elements: (i) an association formed or continued on the basis of a personal relationship, involving mutual confidence—this element will often be found where a pre-existing partnership has been converted into a limited company; (ii) an agreement, or understanding, that all, or some (for their may be 'sleeping' members), of the shareholders shall participate in the conduct of the business; (iii) restriction on the transfer of the members interest in the company—so that if confidence is lost, or one member is removed from management, he cannot take out his stake and go elsewhere.[337]

Louw v. Nel[338] went on to state:

> Generally speaking, an application of this kind, based upon the partnership analogy, cannot succeed if what is complained of is merely a valid exercise of the powers conferred on the majority. To hold otherwise will enable a member to be relieved from the consequences of a bargain knowingly entered into by him.[339]

For, as Trollip JA put it in S*ammel and Others v. President Brand Gold Mining Co. Ltd.*:[340]

> > By becoming a shareholder in a company a person undertakes by his contract to be bound by the decisions of the prescribed majority of shareholders, if those decisions on the affairs of the company are arrived at in accordance with the law, even where they adversely affect his own rights as a shareholder . . . . That principle of the supremacy of the majority is essential to the proper functioning of companies.[341]

In *Visser Sitrus*[342] the Court held:

> [61] On the other hand, the English courts have been anxious to ensure that the remedies should not, as Lord Hoffman[343] (as he had by then become) said, be used as 'a license to do whatever the individual judge happens to think fair' and that one established principle should not be abandoned 'in favour of some wholly indefinite notion of

337. *Ebrahimi* [1972] 2 All ER 492, 500 a-h (emphasis added) (Eng.).
338. *Louw & Others* 2011 (2) SA 172 (SCA) at para. 22.
339. *Id.*
340. *Sammel & Others v. President Brand Gold Mining Co.* 1969 (3) SA 629 (A) at 678 G-H.
341. *Id.*
342. *Visser Sitrus (Pty) Ltd. v. Goede Hoop Sitrus (Pty) Ltd. & Others* 2014 (5) SA 179 (WCD) at para. 61.
343. An English judge of South African origin who sat in the English House of Lords.

> fairness'[344] . . . . The principles of majority rule and the binding nature of the company's constitution remain applicable. As Hoffman LJ said in *Saul D Harrison supra*, 'keeping promises and honouring agreements is probably the most important element of commercial fairness.'[345] The English courts have thus been cautious in extending the remedy beyond cases of illegality . . . .
>
> [62] The learned authors of *Gower & Davies*[346] say that the only clear category which has emerged in England of unfair conduct which is not also illegal (though the jurisdiction is not in law limited to this category) is the case of 'legitimate expectation' or 'equitable consideration' arising from an informal arrangement or understanding among shareholders not contained in the company's constitution . . . . This might be an arrangement or understanding regarding participation in management or concerning dividend policy or remuneration. The arrangement or understanding must be proved as a fact. This makes it difficult to establish a legitimate expectation in cases other than those involving small private companies. The starting point remains the company's articles of association. In the absence of 'something more,' there is no legitimate expectation that the general meeting in the board will not exercise whatever powers they are given by the articles of association . . . .
>
> [63] Similarly, in Canada it has been said that the shareholder expectations that are to be considered in an unfair-prejudice claim are not those 'that a shareholder has as his own individual 'wish list"; the expectations are those 'which could be said to have been (or ought to have been considered as) part of the compact of the shareholders.'[347]

South African courts have been at pains to note that, while a shareholder may have a legitimate expectation that he or she will not be excluded from a say in the management of the company's affairs, the "unfairness disappears if the minority shareholder is offered a fair price for his shares."[348] *Bayly v. Knowles*[349] demonstrates the limits of relief under section 163 of the New Companies Act.[350] In this case, Bayly, a

---

344. *Visser Sitrus (Pty) Ltd.* 2014 (5) SA 179 (WCD) (quoting O'Neill & Another v. Phillips & Others [1999] 2 All ER 961, 966 g-h, 968 a-b) (Eng.).

345. *Re Saul D Harrison & Sons Plc.* [1995] 1 BCLC 14.

346. GOWER, *supra* note 240, at 721-34.

347. Ontario Inc. v. Harold E. Ballard Ltd., [1991] 3 B.L.R. (2d) 113 (Ont. C.J. (Gen. Div.)) at 195-86 (Can.).

348. *Bayly v. Knowles* 2010 (4) SA 548 (SCA) at para. 23; Re a Co., Ex Parte Kremer [1989] BLLC 365 [Ch.1] (Eng.).

349. *Bayly* 2010 (4) SA 548 (SCA) at paras. 22-24.

350. Although the case was decided under section 252 of the Old Companies Act, the principles stated there are similarly applicable to the Companies Act 71 of 2008 § 163.

shareholder and the managing director of a company, offered to buy out his co-shareholder, Knowles, a shareholder in and the sales and marketing director of, Electronic Tracking Systems (ETS), a public company.[351] In addition, if Knowles accepted the offer, he was to resign as a director of ETS.[352] At that point, Knowles and Bayly each held 31.67% of the shares.[353] The next largest shareholder, one M, with 29.17% of the shareholding, had aligned himself with Bayly, which meant that together they held a majority of the equity.[354]

Knowles did not take up the offer but, instead, made a counteroffer that involved, among other things, Knowles being granted a first option to purchase Bayly's shares.[355] The counteroffer was to remain open for two days, after which Knowles would seek the winding up (i.e., dissolution) of ETS.[356] Bayly did not take up Knowles' counteroffer and made it clear that he had no intention of disposing of his shares.[357] From this time threats and demands took over, and as a result of the ongoing conflict between Knowles and Bayly, ETS, which had by then sided with Bayly, had ceased payment of Knowles' salary, suspending all other perks and benefits due to him and excluding him from its business activities by denying access to the company premises.[358]

Knowles alleged oppression and approached the High Court for an order under section 252 of the Old Companies Act reinstating his perks and benefits and restoring his rights of access to ETS' premises.[359] Knowles also gave notice of his intention to seek orders for the sale to him of Bayly's shares and in the alternative an order for the winding up of ETS.[360] Bayly and one M, having made common cause, opposed the application.[361]

The SCA refused to wind up the company or to force Bayly to sell his shares to Knowles.[362] Knowles' application was dismissed.[363] The

---

351. *Bayly* 2010 (4) SA 548 (SCA) at para. 12.
352. *Id.* at para. 13.
353. *Id.* at para. 17 n.3.
354. *Id.*
355. *Id.* at para. 15.
356. *Id.*
357. *Id.* at para. 16.
358. *Id.* at paras. 18, 27.
359. *Id.* at para. 18.
360. *Id.*
361. *Id.*
362. *Id.* at para. 20.
363. *Id.* at para. 30.

Court found that Bayly's offer to Knowles was a *"fair offer."*[364] The court held:

> I am bound to say that certain remarks of Hoffman J . . . in *Re a Company . . . Ex Parte Kremer* act 368 apply four-square to the allegations made by Knowles in this case:
>
> > 'Taken at their face value, these allegations amount at most to highhanded conduct in certain matters. There is nothing in them which can carry a serious imputation of dishonesty. This an ordinary case of breakdown of confidence between the parties. In such circumstances, fairness requires that the minority shareholder should not have to maintain his investment in a company managed by the majority with whom he has fallen out. But the unfairness disappears if the minority shareholder is offered a fair price for his shares. In such a case, s459 was not intended to enable the court to preside over a protracted and expensive contest of virtue between the shareholders and award the company to the winner'[365]
>
> The failure to accept Bayly's offer has important consequences for Knowles. In English law the making of a reasonable offer for the shares of an oppressed minority is enough to counter reliance by the complainer on s 459 of the Companies Act (the equivalent of s 252). Pursuit of the complaint in the face of such an offer is evidence of abuse of the process sufficient to strike out such reliance in limine. The principle of encouraging affected parties to use the procedures provided for in the articles (or in a shareholders agreement) to avoid "the expense of money and spirit" is laudable. In the context of s252 the failure of a minority shareholder to accept a reasonable offer for his shares and leave the company in the hands of the majority is, at least, strong evidence of a willingness to endure treatment which is prima facie inequitable despite the choice of a viable alternative. If this is so it would not ordinarily behoove him to continue to complain about oppression. The rule, however, cannot be absolute In *Re Data v Online Transactions (UK) Ltd* [2003] BCC 510, for example, it was held reasonable for a petitioner to refuse an otherwise acceptable offer where there was not a reasonable prospect that the offeror would be able to meet the financial commitment involved. One can conceive of cases where the offer, although reasonable, may be so tainted by bad faith or ulterior motive as to excuse non-acceptance.[366]

---

364. *Id.* at para. 22.

365. *See* O'Neill & Another v. Phillips & Others 1999 1 WLR 1092HL [1999] 2 All ER 961(Eng.) as approved by the SCA in *Bayly* 2010 (4) SA 548 (SCA) at para. 23.

366. *Bayly* 2010 (4) SA 548 (SCA) at para. 24.

It follows that a majority shareholder confronted with a difficult minority shareholder can usually prevent an action under section 163 of the New Companies Act by making a fair and reasonable offer to buy out the minority shareholder.[367] However, where the very purpose of the oppressive conduct is to squeeze out a minority shareholder who does not wish to be bought out even a fair and reasonable offer will not necessarily ameliorate all oppressive conduct.[368]

B. Winding-Up or Dissolution

The minority shareholder may, instead of applying for relief under section 163 of the New Companies Act, apply to wind the company up in terms of section 81 of the New Companies Act on the basis that it "is otherwise just and equitable for the company to be wound up."[369] "Winding-up" is the process under South African law whereby a company is placed in the hands of a liquidator[370] whose function it is to liquidate the assets of the company.[371] The primary obligation of a liquidator is to realize the assets of the company for the benefit of creditors and, thereafter, for the benefit of shareholders.[372] The liquidator has to realize the assets of the company, pay off its liabilities, and thereafter he may distribute the surplus, if any, to shareholders.[373]

In terms of section 81 of the New Companies Act, a court may order that the company be wound-up on the application of one or more directors or one or more shareholders when:

(i) the directors are deadlocked in the management of the company, and the shareholders are unable to break the deadlock, and
  (aa) irreparable injury to the company is resulting, or may result, from the deadlock; or
  (bb) the company's business cannot be conducted to the advantage of the shareholders generally, as a result of the deadlock;
(ii) the shareholders are deadlocked in voting power, and have failed for a period that includes at least two consecutive annual general meeting dates, to elect successors to directors whose terms have expired; or

---

367. *See id.*
368. *De Villiers v. Kapela Holdings (Pty) Ltd.* 4228I/2015 [2016] ZAGHPJHC278 (14 October 2016) at para. 56 (S. Afr.).
369. Companies Act 71 of 2008 § 81.
370. This is similar to a trustee or receiver.
371. Companies Act 61 of 1973 §§ 386, 390, *read with* Companies Act 71 of 2008 § 79, *and* item 9 of sched. 5.
372. Companies Act 61 of 1973 § 391.
373. *Id.* § 398.

(iii) it is otherwise just and equitable for the company to be wound-up.[374]

The provision that expressly permits a court to wind-up a solvent company on the grounds of deadlock is an innovation in the New Companies Act.[375] The circumstances in which the court will wind the company up on the grounds of deadlock are fairly carefully laid out in section 81(d) and have been set out above.[376] Naturally, a deadlock by its very nature will not usually arise unless warring shareholders have an equal number of voting rights in the company.[377]

It is the provision that the company may be wound-up where it is "just and equitable" to do so that is possibly of particular interest to a minority shareholder.[378] It is not unusual for an aggrieved minority shareholder to seek to have the company wound-up and in the alternative to claim relief under section 163 of the New Companies Act.[379] The threat of a winding-up is a powerful weapon in the hands of the aggrieved minority shareholder.[380] However, as a practical matter, the minority shareholders may chose not to resort to applying for a winding-up because this can have a damaging effect on the company's business.[381] If creditors and customers know that there is a winding-up application pending, they will be less likely to extend credit to the company or to buy from it. The courts have held that the "just and equitable" basis for the winding-up of solvent companies under section 81 of the New Companies Act is the same as that under section 344(h) of the Old Companies Act.[382]

Section 347 of the Old Companies Act expressly provided that the court should not make a winding-up order "unless it is satisfied that some other remedy is available to the applicants and that they are acting unreasonably in seeking to have the company wound up instead of pursuing that other remedy."[383] There is no such express provision in the New Companies Act. Nevertheless, bearing in mind that winding-up should only take place when it is "just and equitable," this limitation

374. Companies Act 71 of 2008 § 81.
375. *See id.*
376. *Id.* § 81(d).
377. *Id.* § 81(ii)
378. *Id.* § 81(iii).
379. *Id.* §§ 81, 161.
380. J. F. CORKERY, DIRECTORS' POWERS AND DUTIES 276 (1987).
381. *Id.* at 267.
382. *Budge v. Midnight Storm Inv. 256 (Pty) Ltd.* 2012 (2) SA 28 (GSG) at para. 12; *Heinrich Muller v. Lily Valley (Pty) Ltd.* [2012] 1 All SA 187 (GSJ).
383. Companies Act 61 of 1973 § 344(h).

should be read into the New Companies Act because it would not be just and equitable to grant a winding-up when the applicant is being unreasonable in pursuing that remedy.[384]

In *Moosa v. Mavjee Bhawan (Pty) Ltd.*,[385] the Court held:

> The history of this piece of legislation[386] assists in understanding and interpreting it. Previously the position was that the availability of some other measure to the applicant to remedy his complaints would usually defeat the application.
>
> Gower on *Modern Company Law*, 2nd Ed, p540 says:
>
> > To wind up a solvent company contrary to the wishes of the majority shareholders is a serious step which the Courts will only take if a strong case is made out. Indeed until the latest Act it was not their practice to do so if any other remedy was available.
>
> And McPherson in the Modern Law Review Article, *supra* at p285 says:
>
> > Indeed the cases themselves suggest that winding-up is always to be regarded as a remedy of last resort, to be granted only when all reasonable alternatives have failed . . . .
>
> But, as Gower at p540, *supra*, dryly comments:
>
> > This makes a winding-up more easily attainable but it does not make it any more inviting. Killing the company is a singularly clumsy method of ending oppression in its operation and it may be suicidal for the petitioner.[387]

South African courts have most commonly in the past granted a winding-up where the company was in essence a partnership or quasi-partnership that had broken down.[388] In those instances, where the relationship of trust and confidence between the quasi-partners/shareholders has broken down but not through the fault of the applicant, the court might grant a winding-up order.[389]

---

384. *Zukiswa Jafta v. Lifu Trading 330 CC* [2013] JOL 30407 (ECG) at para. 49 (S. Afr.); HENOCHSBERG, *supra* note 168, at 332.

385. *Moosa, v. Mavjee Bhawan (Pty) Ltd.* 1967 (3) SA 131 (T) at 150.

386. This is the South African Companies Act 46 of 1952 (i.e., the predecessor to the Old Companies Act).

387. *See* Re Cuthbert Cooper & Sons Ltd. 1937 Ch 392 (Eng.) (a decision of the English Chancery Division approved in *Moosa*); Charles Forte Inv. Ltd. v. Amanda 1964 Ch 240 (Eng.) (as approved by the South African court in *Moosa*) (The court held that proceedings against the company and directors for rectification of the share register would have been an effective and more suitable remedy for the members' complaint. Accordingly, the court refused to grant a winding-up).

388. *Erasmus, v. Pentamed Invs. (Pty) Ltd.* 1982 (1) SA 178 (W) at 181-83.

389. *Id.* at 184.

In *Erasmus v. Pentamed Investments (Pty) Ltd.*,[390] the court summarized the principles to be applied in considering whether to liquidate a company that is in substance a quasi-partnership. In that case, the applicant was a medical practitioner who practiced in partnership with four other doctors.[391] The respondent company was registered by the partnership to acquire immovable property.[392] It was leased by the company to the partnership.[393] The partners acquired shares in the company and became directors.[394] The partnership was dissolved and three of the shareholders gave notice to remove the applicant and one of the others as directors.[395] The applicant applied for the winding-up of the company on the just and equitable ground.[396] The court granted the application on the basis that the exclusion of the applicant from management of the company was a repudiation of the understanding between the shareholders and was in conflict with the state of affairs that was contemplated by them when they entered into the arrangement.[397] The court found that it would be unfair to the applicant to leave him in the company because he never bargained for the situation that had arisen.[398]

In my view, the outcome in *Erasmus v. Pentamed* seems harsh. The company was a property owning company.[399] There is no reason why the court could not have ordered the other shareholders to buy the applicant out at a fair price. It would then have ill-behooved the applicant to contend that it was unfair for him to be forced to sell out while the others were entitled to retain their shares. This is because the liquidation would in any event have resulted in the property being put up for sale.

An analysis of more recent decisions suggests that modern courts are more reluctant to order a liquidation because of its dire economic consequences.[400] For example, in *Bayly v. Knowles*,[401] the applicant had also been removed from his position as a director of the company. However, the SCA refused to grant a liquidation because: (1) the

390. *Id.* at 181 A-185 E.
391. *Id.* at 178 C-D.
392. *Id.*
393. *Id.*
394. *Id.*
395. *Id.* at 178 C-D.
396. *Id.* at 178 D.
397. *Id.* at 178 F.
398. *Id.* at 190 A-D.
399. *Id.* at 178 C-D.
400. *See*, *e.g.*, *Bayly v. Knowles* 2010 (4) SA 548 (SCA) at 557 G-I.
401. *Id.*

majority shareholders had made a fair offer to buy out the applicant's shares; and for the following reasons:

> (2) "liquidation would destroy a perfectly viable company . . . but, in doing so, it would provide no redress to [the applicant] for such oppression as he may have suffered. The first consequence is one that a court will avoid, except in most extraordinary circumstances; the second would favour revenge above reason—financially [the applicant] might even be prejudiced by sale in liquidation.[402]

VI. CONCLUSION

The statutory aspects of South African company law are laid out with reasonable clarity in the New Companies Act.[403] The New Companies Act is backed by a consistent body of common law authorities that are easily accessible to both local and foreign legal practitioners.[404] The corporate structure and the rights and remedies of shareholders and directors is based heavily on English case law that has been repeatedly endorsed by South African courts.[405]

South African company law governing the rights and obligations of shareholders and directors has many areas of commonality with the law of most American states.[406] Directors are required to observe the standards of skill and diligence comparable to those of company directors in the United States and in England.[407] Directors will not usually be held liable for a failure of business judgment where they have exercised their powers in good faith and for a proper purpose, in the best interests of the company and with the degree of care, skill, and diligence that may reasonably be expected of persons with the director's level of skill charged with the particular task that the director is required to perform.[408]

A director can be held liable to both shareholders and creditors for damage caused to them arising out of reckless or fraudulent trading.[409] Where the company has been placed in liquidation, it would not be necessary for a creditor to prove that the conduct of the director actually

---

402. *Id.* at para. 29.
403. *See* Companies Act 71 of 2008.
404. CASSIM ET AL., *supra* note 7, at 2-3.
405. *Id.* at 17-18.
406. *See* Miller v. Am. Tel. & Tel. Co., 507 F.2d 759, 762 (3d Cir. 1974); Guth v. Loft, 5 A.2d 503 (Del. 1939).
407. *See*, *e.g.*, *Guth*, 5 A.2D 503.
408. *See Miller*, 507 F.2d at 762.
409. *See Philotex (Pty) Ltd. v. Snyman* 1998 (2) SA 138 (SCA) at 186 A-D.

caused damage to the plaintiff.[410] The liability of directors and shareholders to each other is financially finite.[411] South African law does not allow punitive damages.[412] Moreover, damages must be proved on a sum formula basis—that is to say, a plaintiff has to prove that he or she has suffered loss in the actual amount of compensation awarded.[413]

Oppressed minority shareholders have a number of statutory equitable remedies that afford the court wide discretion to redress oppressive or unfairly prejudicial conduct by a majority shareholder or the directors.[414] The most common remedy afforded a disgruntled shareholder is ordering a buyout of his or her shares at a fair price.[415] This can take into account any damage to the value of the minority shareholder's shares resulting from the oppressive or unfairly prejudicial conduct about which the plaintiff complains.

410. *Bayly v. Knowles* 2010 (4) SA 548 SCA at para. 30.
411. *Jones v. Krok* 1996 (1) SA 504 (T) at 515 G-H.
412. *See id.*
413. *See* VISSER ET AL., *supra* note 11, at 72-73.
414. *See Bayly* 2010 (4) SA 548 SCA at para. 30.
415. *See id.*