SOUTH AFRICAN PRINCIPLES OF CORPORATE GOVERNANCE: LEGAL AND REGULATORY RESTRAINTS ON POWERS AND REMUNERATION OF EXECUTIVE DIRECTORS

by

NOMUSA JANE MOYO

Submitted in fulfillment of the requirements for the degree of

Master of Laws

at the

UNIVERSITY OF SOUTH AFRICA

SUPERVISOR: PROF IRENE-MARIÉ ESSER

NOVEMBER 2010

TABLE OF CONTENTS

DEDICATION V

ACKNOWLEDGEMENTS VI

DECLARATION VII

CHAPTER 1 1

INTRODUCTION 1

1.1 BACKGROUND TO THE RESEARCH 1

1.2 PURPOSE OF STUDY 4

1.3 DEFINITION OF CORPORATE GOVERNANCE 4

1.4 IMPORTANCE OF CORPORATE GOVERNANCE 8

1.5 ASSUMPTIONS OF THE RESEARCH 13

1.6 THE FRAMEWORK OF THE DISSERTATION 13

1.7 RESEARCH METHODS 15

1.8 REFERENCE TECHNIQUES 15

CHAPTER 2 16

CORPORATE GOVERNANCE IN SOUTH AFRICA 16

2.1 DUTIES AND POWERS OF DIRECTORS 16

2.1.1 Introduction 16
2.1.2 Duty to Act in Good Faith 18
2.1.2.1 Conflict of Interest 19
2.1.2.1.1 Common Law 19
2.1.2.1.2 Companies Act 61 of 1973 21
2.1.2.1.3 Companies Act 71 of 2008 22
2.1.2.1.4 The Johannesburg Securities Exchange Listings Requirements 24
2.1.2.2 Duty Not to Exceed the Limitation of Their Power 24
2.1.2.2.1 Common Law and Companies Act of 61 of 1973 24
2.1.2.2.2 Companies Act 71 of 2008 26
2.1.2.3 Unfettered Discretion and Proper Purpose 28
2.1.2.3.1 Common Law 28
2.2.1.3.2 The Companies Act 29
2.1.3 Duty of Care, Skill and Diligence 30
2.2.2.1 Common Law 30
2.1.3.2 Companies Act 61 of 1973 34
2.1.3.3 Companies Act 71 of 2008 35
2.1.3.4 King Report 36
2.1.3.5 Johannesburg Securities Exchange (JSE) Listing Rules 37
2.1.4 Conclusion 38

2.2 SOUTH AFRICAN CORPORATE GOVERNANCE LEGAL AND REGULATORY MECHANISMS 39

2.2.1 Introduction 39
2.2.2 King Code on Corporate Governance 41

المنارة للاستشارات
www.manaraa.com

2.2.2.1 Introduction ... *41*
2.2.2.2 Role and Function of the Board ... *46*
2.2.2.3. Appointment of New Directors ... *47*
2.2.2.4 Composition of the Board ... *47*
2.2.2.5 Separation of Chief Executive Officer (CEO) and Chairman's Roles ... *49*
2.2.2.6 Board Committees ... *50*
2.2.2.7 Compliance with Laws, Rules, Codes and Standards ... *51*
2.2.2.8 Shareholder Participation ... *52*
2.2.2.9 Conclusion ... *53*
2.2.3 THE COMPANIES ACT ... 54
2.2.3.1 Introduction ... *54*
2.2.3.2 Codification of Directors' Duties ... *56*
2.2.3.3 Board Committees ... *58*
2.2.3.4 Shareholder Participation ... *59*
2.2.3.5 Conclusion ... *61*
2.2.4 OTHER ACTS ... 61
2.2.4.1 Introduction ... *61*
2.2.4.2 Securities Services Act 36 of 2004 ... *62*
2.2.4.3 Public Finance Management Act 1 of 1999 ... *64*
2.2.4.4 Broad-Based Black Economic Empowerment Act 53 of 2003 ... *65*
2.2.4.5 Conclusion ... *67*
2.2.5 THE JSE LISTINGS REQUIREMENTS ... 67
2.2.5.1 Introduction ... *67*
2.2.5.2 Corporate Governance Related Listing Requirements ... *69*
2.2.6 REMUNERATION OF DIRECTORS ... 70
2.2.6.1 Introduction ... *70*
2.2.6.2 King Code on Corporate Governance ... *72*
2.2.6.2.1 Remuneration Committee ... 72
2.2.6.2.2 Disclosure of Directors' Remuneration ... 73
2.2.6.2.3 Shareholder Approval of Directors Remuneration ... 74
2.2.6.3 The Companies Act ... *75*
2.2.6.3.1 Introduction ... 75
2.2.6.3.2 Shareholder Approval of Remuneration ... 76
2.2.6.3.3 Disclosure of Remuneration ... 77
2.2.6.4 JSE Listings Requirements ... *78*

2.2.7 ENFORCEMENT MECHANISMS ... 80

2.2.7.1 King Code ... *80*
2.2.7.2 The Companies Act ... *82*
2.2.7.3 JSE Listing Requirements ... *86*
2.2.7.4 Regulatory Bodies ... *87*
2.2.8 CONCLUSION ... 90

CHAPTER 3 ... 92

EVALUATION OF SOUTH AFRICAN CORPORATE GOVERNANCE MECHANISMS ... 92

3.1 INTRODUCTION ... 92

3.2 ASSESSMENT OF EFFECTIVENESS OF CORPORATE GOVERNANCE FRAMEWORK ... 93

3.2.1 WEAK ENFORCEMENT AND PROSECUTION ... 93
3.2.2 INSUFFICIENT BOARD INDEPENDENCE AND BALANCE OF POWER ... 99
3.2.3 SHAREHOLDER PASSIVITY ... 101
3.2.4 CORRUPTION ... 102
3.2.5 INSUFFICIENT DISCLOSURE OR REPORTING ... 103

المنارة للاستشارات
www.manaraa.com

3.3 CONCLUSION **105**

CHAPTER 4 ..... **107**

COMPARISON BETWEEN SOUTH AFRICAN AND UNITED KINGDOM CORPORATE GOVERNANCE LAWS AND REGULATIONS **107**

4.1 INTRODUCTION **107**

4.2 COMPANY LAW - DUTIES OF DIRECTORS **109**

4.3 RECENT DEVELOPMENTS IN CORPORATE GOVERNANCE **112**

4.4 APPLICATION OF CORPORATE GOVERNANCE CODES **115**

- **4.4.1 Composition of the Board** 117
- **4.4.2 Separation of Chief Executive Officer (CEO) and Chairman's roles** 119
- **4.4.3 Role and function of the board** 119
- **4.4.4 Shareholders Participation** 120
- **4.4.5 Remuneration of Directors** 122

4.5 ENFORCEMENT OF COMPLIANCE **125**

4.6 CONCLUSION **129**

CHAPTER 5 ..... **131**

SUMMARY, CONCLUSION AND RECOMMENDATIONS **131**

5.1 INTRODUCTION **131**

5.2 SUMMARY OF FINDINGS **132**

5.3 CONCLUSIONS **137**

5.4 RECOMMENDATIONS **139**

- **5.4.1 Induction and training of directors** 140
- **5.4.2 Name and shame approach** 141
- **5.4.3 Improve Enforcement Mechanisms** 142
- **5.4.4 Encourage Shareholders Participation** 143
- **5.4.5 Enhance the effectiveness of non-executive directors** 144
- **5.4.6 Develop Guidelines on Executive Remuneration** 145
- **5.4.7 Improve quality of information in accounts and reports** 146

BIBLIOGRAPHY **148**

المنارة للاستشارات
www.manaraa.com

DEDICATION

To my children; Faith, Primrose and Isheanesu

المنارة للاستشارات

www.manaraa.com

ACKNOWLEDGEMENTS

I gratefully acknowledge and extend my sincere gratitude to the following without whose input this research would not have been successful:

God the Almighty for the everlasting love, grace, blessings, wisdom and guidance;

Professor Irene-Marié Esser, under whose supervision the research was conducted, for her unwavering support, valuable comments, constructive criticism and extensive guidance in directing the completion of this work;

My beloved children; Faith, Primrose and Isheanesu, whom I neglected so much whilst carrying out this research;

My parents, brothers, sisters and friends for their prayers and motivation in helping me achieve this landmark in my life;

Last but not least, my warm appreciation to my husband Edson Moyo for his encouragement, dependable support and endurance.

المنارة للاستشارات
www.manaraa.com

STUDENT NUMBER: 3599-385-5

DECLARATION

I Nomusa Jane Moyo declare that **'South African Principles of Corporate Governance: Legal and Regulatory Restraints on Powers and Remuneration of Executive Directors'** is my own work and that all the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

N. J Moyo ……………………………….. ………………

Signature Date

المنارة للاستشارات
www.manaraa.com

SUMMARY

The corporate governance set-up in South Africa has undergone fundamental changes during the past decade, with the country today being responsive to most corporate governance issues. South Africa should be complimented for its *King Code on Corporate Governance*, the Companies Act and *Johannesburg Securities Exchange Listing Requirements* which have significantly strengthened the country's corporate governance framework. These legal instruments have been influential in limiting directors' powers and regulating the way directors are remunerated as a way of achieving good corporate governance.

The research discusses the South African corporate governance framework with particular focus on the legal and regulatory framework that seeks to regulate directors' powers and remuneration. An evaluation of the extent to which the legal and regulatory framework restrains directors' powers and curbs excessive remuneration is undertaken. Recommendations are then provided on how the existing framework can be improved to adequately and effectively regulate directors' powers and remuneration so as to achieve good corporate governance.

KEY TERMS

good corporate governance, executive directors, restrain, directors' duties, regulatory, *King Report*, Companies Act, *JSE Listing Requirements*, directors' powers, excessive remuneration.

المنارة للاستشارات
www.manaraa.com

CHAPTER 1

INTRODUCTION

1.1 Background to the Research

Corporate governance[1] is important for ensuring that certain individuals in an organisation are held accountable and that organisations are properly directed and controlled. In recent times corporate governance has drawn wide attention partly due to corporate collapses of prominent corporations both in South Africa and internationally[2] and partly from the growing responsiveness to the need for good practice to attract investment capital.[3] Among the reasons for most of the corporate collapses is the abuse of power and fraudulent dealings of directors on one hand, and the weak link between directors' remuneration and company performance on the other hand.[4] Much of the corporate collapses have thus been a result of self seeking activities of too powerful company directors, their apparent lack of personal and business ethics and the inability of their contemporaries on the board to restrict them from acting improperly.[5] With some corporate collapses, the failure has been attributed to a dominant individual, acting as

[1] The term corporate governance is defined and the importance of corporate governance is discussed in paragraphs 1.3 and 1.4 respectively below.

[2] Examples of some of the corporate collapses which have resulted in wider attention being drawn towards company directors' actions, skill and diligence are Enron Corporation and Worldcom in the United States of America and Fidentia, Masterbond, Regal Treasury Bank and LeisureNet in South Africa (Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 20 *South African Mercantile Law Journal 95*–116.).

[3] The research focuses particularly on executive directors' powers and remuneration and their adverse contribution to corporate collapses hence only a brief discussion is made in paragraph 1.4 on the importance of corporate governance in attracting investment capital.

[4] Langtry S, *Corporate Governance,* A Discussion Paper to Assist with the Preparation of South Africa's African Peer Review Mechanism (APRM) Self Assessment Report, *(*2005) available at www.aprm.org.za/docs/APRMOpinionPiece-Corporate _Governance (visited on 19 August 2009).

[5] Coyle B, *Corporate Governanc*e, (ICSA Publishing Ltd 2003) 8-10.

المنارة للاستشارات
www.manaraa.com

chairman and chief executive, running the company as a personal kingdom and with complete disregard to the interests of shareholders and other stakeholders.[6]

Concerns about corporate governance have also arisen out of investor anxiety about excessive powers in the hands of greedy executive directors who seek to get the best for themselves out of their companies.[7] This is mostly because directors' remuneration has tended to rise rapidly regardless of company performance, whereas a principle of good corporate governance is that remuneration should be linked, to some extent, to company performance[8] so that a director will earn more if the company does well, and less if it performs badly.[9] Contrary to this governance principle, research results have confirmed that the director's fiduciary duty owed to the company is not compatible with some of the extravagant pay packages enjoyed by some executive directors.[10]

Corporate governance thus requires that directors use their powers in ways that are best for the company and its shareholders and that they receive appropriate remuneration in line with the firm's performance and corporate governance policy.[11] It therefore, ensures

[6] An example of a company managed this way is the Polly Peck International case. Polly Peck was a company that was run by a single individual, Mr. Asil Nadir, who was both board chairman and chief executive officer. Because of poor systems of internal controls Mr. Nadir managed to transfer large amounts of money from the company's bank accounts to his personal accounts without any questions being asked resulting in the collapse of the company. See also Clieaf V, Executive Accountability and Excessive Compensation: A New Test for Director Liability, (2004) *The Corporate Governance Advisor* 12(6) 2-5.

[7] Clieaf V, Executive Accountability and Excessive Compensation: A New Test for Director Liability, *(*2004) 1-4. Until the late 1990s directors' remuneration was not seen as a major problem of corporate governance but the issue attracted attention when the general public, informed by the media, criticised some top executives for being paid far more than they are worth and when investment institutions criticised directors for receiving increasing rewards even when their companies were not performing well. (Marcotti A. G, *Fiduciary Duty and Directors' Pay,* The Times, 13 March 2009, 4)

[8] Chapter 2 of the *King II Report on Corporate Governance 2002* (hereinafter referred to as *King II*) and chapter 2 of the *King III Report on Corporate Governance 2009* (hereinafter referred to as *King III*).

[9] Coyle B, *Corporate Governanc*e, (2003) 133.

[10] Plumptre T, *The New Rules of the Board Game*, *The Changing World of Corporate Governance and its Implications for Multilateral Development Institution*, Institute on Governance, Ottawa, (2004), available at www.iog.ca (visited on 6 June 2009).

[11] Talha M, Salim A S A, Masoud S, A study on Directors' Remuneration and Board Committee in Malaysia*,* (2009) *USA Journal of Modern Accounting and Auditing*, ISSN1548-6583, Vol.5(1) (Serial No.44) 34-35. Corporate governance principles seek to limit directors' powers so that they are not abused. Limitations of directors' powers take various forms as discussed in chapter 2 below. See for example section 76 of the Companies Act 71 of 2008 that requires a director to act 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 him. Similarly sections 221-228 of the

المنارة للاستشارات
www.manaraa.com

that shareholders' investment is not put at risk by providing for reasonable limits to the powers of executive directors who may seek to further their own interests at the expense of the company and other stakeholders.[12] In a well-governed company, there should thus be checks and balances that prevent one individual or group of executive directors from dominating the board and its decisions.[13]

The foregoing makes it imperative to analyse and evaluate the extent to which South African legislatures and committees[14] have intervened to address the adverse effects of abuse of executive directors' powers and payment of excessive remuneration. Research has shown that legislatures and committees have intervened, through laws and regulations, which have worked in the interests of shareholders and other stakeholders.[15] Despite the presence of such a regulatory framework, there remain some inherent grey areas[16] that executive directors exploit in advancing their own interests at the expense of shareholders and other interested parties thus resulting in corporate failure as signified by the continued corporate failures.[17]

Companies Act 61 of 1973 place restrictions on the powers of directors and sections 234-241 place a duty on directors to disclose any interests in contracts. It is also a well established rule of company law that directors have a fiduciary duty to act in good faith and in the best interests of the company. This rule was confirmed in *Robinson v Randfontein in Estates Gold Mining Co Ltd* 1921 AD 168 where it was held that directors may not make a secret profit or otherwise place themselves in a position where their fiduciary duties conflict with their personal interests.

[12] Leisurenet is one such case where executive directors abused their powers and cared more about their own welfare than for those that entrusted their money to them. LeisureNet was a lifestyle and health fitness company, which had a board comprising some of South Africa's most respectable non-executive directors but collapsed in 2000, allegedly because of fraud committed by the two key executives and part-owners, losing some R1.2 billion. (Langtry S, *Corporate Governance,* (2005) 15).

[13] Coyle B, *Corporate Governanc*e, (2003) 63-64.

[14] For example the King Committee on corporate governance.

[15] Armstrong P, Segal N and Davis B, Corporate Governance: South Africa, a Pioneer in Africa*, Global Best Practice, Report No. 1*, *The South African Institute of International Affairs, (*Johannesburg 2005) 14-17.

[16] These areas are discussed below in chapter 4.

[17] The 2002 Saambou Bank Limited failure, which involved allegations of criminal conduct by top company executives implicated in perhaps the biggest insider trading in South African history, is one such example which occurred after the introduction of the *King Report on Corporate Governance for South Africa 1992* (hereinafter referred to as *King I*).

المنارة للاستشارات
www.manaraa.com

1.2 Purpose of Study

The main problem to be examined in this study is to establish what corporate governance framework South Africa has put in place since the introduction of the *King I Report* and to assess the effectiveness of the framework with particular reference to directors' powers and remuneration.

Essentially, the research discusses the South African corporate governance framework with particular focus on the legal and regulatory framework that is in place to enhance good corporate governance in so far as directors' powers and remuneration are concerned. Recommendations are then provided on how the existing framework can be improved to adequately and effectively restrain directors' powers and regulate their remuneration so as to achieve good corporate governance.

Given the comparative value of the South African and United Kingdom's legal systems, the research will also compare and contrast the two countries' corporate governance laws and regulations in as far as directors' powers and remuneration are concerned.

1.3 Definition of Corporate Governance

The term "corporate governance" is susceptible to both broad and narrow definitions. In fact, many of the codes on corporate governance do not even attempt to articulate what is encompassed by the term.

The *Cadbury Report*[18] defines corporate governance "as the system by which companies are directed and controlled" and as therefore referring to all aspects of the control and management of companies. The definition is still considered by many as the most authoritative and from a legal point of view, a paramount description of what corporate

[18] Sir Cadbury A, Committee on Financial Aspects of Corporate Governance, *Final Report and Code of Best Practice* (December 1992) par 2.5.

المنارة للاستشارات
www.manaraa.com

governance really is.[19] The most significant feature of Cadbury's view is that it focuses almost exclusively on the internal structure and operation of the corporation's decision-making process.[20] Furthermore, it relates to the interrelationship between a company's management, its board, its shareholders and other stakeholders; provides the structure through which objectives of the company are set; and places a strong emphasis on the welfare of shareholders.[21] It therefore, incorporates matters such as directors' duties, financial accounting, and the protection of the interests of various stakeholders.[22]

The Organisation for Economic Cooperation and Development (OECD) Task Force defines corporate governance as follows:

> *"Corporate governance ... involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders and should facilitate effective monitoring, thereby encouraging firms to use resources more efficiently."*[23]

From this definition, corporate governance seeks to ensure that an organisation achieves its strategic goals over the long-term by meeting the needs of all its stakeholders.[24] Corporate governance also entails that a company and especially its directors abide by the provisions of company law as well as other statutes and manage the company

---

[19] Horn R C, The *Legal Regulation of Corporate Governance with Reference to International Trends*, Published LLM Thesis, (University of Stellenborsh 2005) 9.

[20] Salacuse J W, Corporate Governance in the New Century, (2004) *The Company Lawyer* 25(3) 69-83.

[21] Du Plessis J J, Corporate Governance and the Cadbury Report, (1994) 6 *South African Mercantile Law Journal* 81-82.

[22] Ibid.

[23] OECD Principles of Corporate Governance, (OECD, April 1999) available at http://www.oecd.org/dataoecd/32/18/31557724.pdf, (visited on 20 June 2009).

[24] Wixley T. & Everingham G, *What You Must Know About Corporate Governance*, (Cape Town: Siber Ink CC 2002) 1-3.

المنارة للاستشارات
www.manaraa.com

reliably.[25] The OECD definition encompasses not only internal aspects of corporate governance but takes into account other stakeholders and the impact of the company on them.

A business author, Gabrielle O'Donovan defines corporate governance as:-

> "*an internal system encompassing policies, processes and people, which serves the needs of shareholders and other stakeholders, by directing and controlling management activities with good business savvy, objectivity, accountability and integrity. Sound corporate governance is reliant on external marketplace commitment and legislation, plus a healthy board culture which safeguards policies and processes.*"[26]

According to O'Donovan, corporate governance is a system of structuring, operating and controlling a company with a view to achieve long term strategic goals to satisfy shareholders, creditors, employees, customers and suppliers, and complying with the legal and regulatory requirements, apart from meeting environmental and local community needs.[27] From a different perspective, the Securities and Exchange Board of India (SEBI) committee on Corporate Governance[28] views corporate governance as about ethical conduct in business in that it is concerned with the code of values and principles that enables a person to conduct a company's business in line with the expectations of all stakeholders.[29] According to the committee "corporate governance is

---

[25] Van der Merwe J. G, Appleton R. B, Delport P. A, Furney R. N, Mahony D. P, Koen M, *South African Corporate Business Administration*, (Juta & Co Ltd 2009) 15.1-15.32.

[26] O'Donovan G, A Board Culture of Corporate Governance, (2003) *Corporate Governance International Journal* Vol 6(3) 22-30.

[27] Ibid.

[28] *Report of the SEBI Committee on Corporate Governance*, February 2003, available at http://www.acga-asia.org/public/files/India_MurthyCtee_Feb03.pdf (visited on 7 October 2009).

[29] The SEBI Committee defines corporate governance as "the acceptance by management of the inalienable rights of shareholders as the true owners of the corporation and of their own role as trustees on behalf of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal & corporate funds in the management of a company." (*Report of the SEBI Committee on Corporate Governance*, (2003) 1.)

المنارة للاستشارات
www.manaraa.com

beyond the realm of law. It stems from the culture and mindset of management, and cannot be regulated by legislation alone."[30]

An analysis of the above definitions tempts one to come to the conclusion that corporate governance is more important in large companies where the separation of ownership from management is much more pronounced than for small private companies. This is so because most public companies raise capital on the stock market and institutional investors who hold the vast portfolios of shares and other investments need a guarantee that their investments are reasonably safe. Therefore, if the integrity of the directors in charge of the company's affairs is questionable, the value of the company's shares will be adversely affected and the company will find it difficult to raise new capital.[31] Likewise, where a country does not practice good corporate governance, the country will encounter challenges in attracting foreign investment.[32]

However, many of the issues of corporate governance also apply to smaller companies and to non-corporate organisations, such as state-owned enterprises, government departments, institutes and charitable organisations.[33] A government organisation for instance, should be run in the interests of the general public and in pursuit of the aims of the government itself. Similarly, a charitable organisation should be managed in the interests of the charitable activity and with regard to the interests of and concerns of providers of the funding. Irrespective of the type of ownership and structure, the wider governance agenda advocates that all organisations should act ethically and in a socially responsible manner.[34] Individuals controlling an organisation should thus work for the

[30] *Report of the SEBI Committee on Corporate Governance*, (2003) 1.

[31] Coyle B, *Corporate Governance*, (2003) 89.

[32] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 96.

[33] This is confirmed in the *King III* which, unlike its predecessors, applies to all entities regardless of their nature, size or form of incorporation or establishment.

[34] Coyle B, *Corporate Governance*, (2003) 5-6.

المنارة للاستشارات
www.manaraa.com

objectives of the organisation and should not permit self-interest to dominate their decisions.

1.4 Importance of Corporate Governance

Corporate governance is a multi-faceted subject whose important theme is to ensure the accountability of certain individuals in an organisation through mechanisms that try to reduce or eliminate the so called principal-agent problem.[35] According to Okeahalam and Akinboade (2003), the need for corporate governance arose mainly from the principal-agent problem, primarily because of the separation of management and ownership in modern business.[36] This separation causes potential conflicts of interests between management and investors because the interests of shareholders and directors do not always coincide.[37]

In support of this, the American Bar Association (ABA)[38] stipulates that directors of companies may sometimes succumb to the temptation of serving their personal interests by maximising their own wealth or control through manipulating or misreporting of corporate information, at the expense of the long term well being of the organisation. They may be inclined to report good news and downplay business setbacks or mistakes out of selfish concerns where such reports might expose their poor performance.[39] These concerns were clearly evident in the Enron debacle where the chief executives defrauded the company by falsifying its publicly reported financial statements and also making

---

[35] Emery D R, Finnerty J D and Stowe J D, *Corporate Financial Management*, 2nd Edition, (Upper Saddler River 2004) 374-381.

[36] Okeahalam C C and Akinboade O A, *A Review of Corporate Governance in Africa: Literature, Issues and Challenges*, a paper presented for the Global Corporate Governance Forum on 15 June 2003 available at http://www.ifc.org/ifcext/cgf.nsf/AttachmentsByTitle/Pan_Africa_2003_Review_of_CG_Okeahalam/$FILE/Charles+Okehalam+-+Corporate-Governance+ver+4+Jul+2003.pdf. (visited on 27 September 2009).

[37] Jensen M and Meckling W, Theory of Firm: Managerial Behavior, Agency Costs and Ownership Structure, (1996) *Journal of Economics* 3(4) 305-360.

[38] American Bar Association (ABA), *Report of the Task Force on Corporate Responsibility*, February 2002, available at: http//www.abanet.org/buslaw/corporateresponsibility/finalreport.pdf, (visited on 29 August 2009).

[39] Ibid.

المنارة للاستشارات
www.manaraa.com

false and misleading public representations concerning the company's business performance and financial position.[40] On the other hand, Enron's lawyers were accused of approving potentially fraudulent transactions and conducting an investigation viewed largely as a cover up.[41] In a bid to check such potentially harmful intentions and to orient directors towards the interests of the organisation and its shareholders, corporate governance principles were born.[42]

However, it should be noted that the need for corporate governance is more complex than this and extends far beyond resolving problems stemming from the separation of ownership and control. The challenge of corporate governance therefore, becomes to find a way in which the interests of shareholders, directors and other interested parties can all be sufficiently satisfied. Many of the guidelines in the codes of conduct for corporate governance and the codes of best practice, for example the South African *King Reports*,[43] the OECD corporate governance guidelines[44] and the United Kingdom *Combined Code*,[45] are directed towards reducing the potential for conflict between shareholders and directors by seeking to put some restraints on directors' powers and by also trying to reconcile the interests of the two stakeholder groups.[46] Corporate governance principles should thus, to a certain extent, curtail the excessive concentration

---

[40] Securities Exchange Commission, *SEC Charges Kenneth L Lay, Enron's Former Chairman and CEO with Fraud and Insider Trading*, 2004, available at http//www.sec.gov/news/press/2004-94.htm, (visited on 15 July 2009).

[41] Fisch J E and Rosen K M, Is there a Role for Lawyers in Preventing Future Enrons? (2003) *Villanova Law Review*, Vol 48, 1097-1099.

[42] Okeahalam C.C and Akinboade O.A, *A Review of Corporate Governance in Africa: Literature, Issues and Challenges*, (2003) 8-10.

[43] These are the *King I Report on Corporate Governance 1992, King II Report on Corporate Governance 2002* and *King III Report on Corporate Governance*. These are available at www.iodsa.co.za.

[44] The OECD Principles of Corporate Governance were endorsed by OECD Ministers in 1999 and have since become an international benchmark for policy makers, investors, corporations and other stakeholders worldwide. They are available at www.oecd.org/dataoecd/32/18/31557724.pdf.

[45] The *Combined Code* on Corporate Governance was a result of an amalgamation of the *Cadbury* and *Greenbury Reports* which were brought together in 1998 in United Kingdom. The Code was updated in 2003 and is available at: www.fsa.gov.uk/pubs/ukla/lr_comcode2003.pdf.

[46] United Nations Conference on Trade and Development, *Guidance on Good Practices in corporate Governance Disclosure,* United Nations, New York and Geneva, 2006 available at: http://www.unctad.org/en/docs/iteteb20063_en.pdf. (visited on 20 June 2009).

المنارة للاستشارات
www.manaraa.com

of power in the hands of directors so that no one individual has unfettered powers or authority.

According to Lipman:

> *"Good corporate governance helps to prevent corporate scandals, fraud, and potential civil and criminal liability of the organisation. A good corporate governance image enhances the reputation of the organisation and makes it more attractive to customers, investors, suppliers, and in the case of non-profit organisations, contributors*."[47]

Experience over the last decade has clearly shown that in emerging market economies, successful privatisations and the development of vibrant private sectors depend, to a significant extent, on the existence of effective systems of corporate governance. Generally, the ability of countries to attract foreign capital is affected by their systems of corporate governance and the degree to which corporate management is compelled to respect the legal rights of shareholders and other stakeholders.[48] Individual and institutional investors will refrain from providing capital or will demand a higher risk premium for their capital from enterprises in countries without effective systems of corporate governance than from similar enterprises in countries having strong corporate governance standards.[49] International investment thus not only provides corporations with expanding sources of capital, but also encourages the continued integration of sound corporate governance practices, which may help the corporations to gain the trust of investors, reduce their capital costs and induce more stable financial sources.[50] In addition to the above, Mervyn King argues that corporate governance principles ensure

---

[47] Lipman F D. & Lipman L K, *Corporate Governance Best Practices: Strategies for Public, Private, and Not-for-Profit Organizations*, (New Jersey: John Wiley & Sons 2006) 3.

[48] Horn R C, The *Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 15-16.

[49] Salacuse J W, Corporate Governance in the New Century, (2004) 69-83.

[50] Vaughn M and Verstegen Ryan L, Corporate Governance in South Africa: a Bellwether for the Continent? (2006) *Corporate Governance: An International Review,* Vol. 14(5) 504-512.

المنارة للاستشارات
www.manaraa.com

that directors are held accountable to capital providers for the use of assets and act in the best interests of the company.[51]

Arthur Levitt, the former United States Securities and Exchange Commissioner is quoted to have said the following on the importance of corporate governance:

> "*If a country does not have a reputation for strong corporate governance practices, capital will flow elsewhere. If investors are not confident with the level of disclosure, capital will flow elsewhere. If a country opts for lax accounting and reporting standards capital will flow elsewhere. All enterprises in that country regardless of how steadfast a particular company's practices may be, suffer the consequences. Markets exist by the grace of investors and it is today's more empowered investors who will determine which companies and which markets will stand the test of time and endure the weight of greater competition. It serves as well to remember that no market has a divine right to the investor's capital*."[52]

From Levitt's comments, the degree to which corporations observe basic principles of good corporate governance is an important factor for investment decisions. Good corporate governance is a necessity for today's complex and dynamic business environment to ensure long-term sustainability. It should thus be cultivated and practiced regularly within the business structure. International awards for good corporate behaviour may be instituted, but if corporations and other businesses ignore the lessons that companies like Enron, WorldCom, Masterbond, Regal Treasury Bank and LeisureNet have to offer, they will fail to regain the public trust that is so essential to their long-term success and survival.[53]

In summary, countries and businesses that genuinely recognise and embrace the principles of "good governance" will derive enormous benefits. Firstly, corporate governance helps companies and economies attract investment and strengthen the

[51] Introduction and Background to the *King II and III*.

[52] Introduction and Background to the *King II*.

[53] Shil N. C, Accounting for Good Corporate Governance, (2008) *JOAAG*, Vol. 3(1) 29-30.

المنارة للاستشارات
www.manaraa.com

foundation for stable and long-term economic performance and international competitiveness in several ways.[54] Secondly, at the company level, strong corporate governance permits judicious use of resources, enables an organisation to maximise the opportunities available to it, manage its risks better, boost its chances of succeeding in the market and to achieve truly sustainable long term growth.[55] Thirdly, corporate governance procedures improve the management of the firm by helping firm managers and boards to develop a sound company strategy, and by ensuring that mergers and acquisitions are undertaken for sound business reasons, and that compensation systems reflect performance. This helps companies to attract investment on favorable terms and enhances firm performance.[56]

Fourthly, corporate governance specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.[57] Last but not least, good corporate governance also helps ensure that corporations take into account the interests of a wide range of constituencies, as well as of the communities within which they operate.[58]

However, it appears that the impulsion for continual development of corporate governance codes of best practice and stricter regulatory regimes is mostly a result of scandals and corporate collapses that continue to emerge following directors' unethical

---

[54] McKinsey and Company, *Investor Opinion Survey on Corporate Governance* (June 2000), available at www.oecd.org/dataoecd/56/7/1922101.pdf (visited on 12 August 2009).

[55] Horn R. C, The *Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 15-17.

[56] La Porta R, Lopez De Silanes F, Shleifer A, and Vishny R, Legal Determinants of External Finance, (1997) *The Journal of Finance*, 52(3) 1131-1150.

[57] The Organization of Economic Cooperation and Development Principles of Corporate Governance available at www.oecd.org. (visited on 20 June 2009).

[58] *Report of the SEBI Committee on Corporate Governance,* (2003) 1.

المنارة للاستشارات
www.manaraa.com

conducts, abuse of power and bad corporate governance practices.[59] The need to restore public trust, stimulate economic development and the demands for greater accountability by investors, many of whom lost vast sums of money in the wake of the misappropriation of corporate funds, have also contributed to the heightened attention that has been given to the importance of corporate governance.[60] Corporate governance thus provides for checks and balances to prevent directors from abusing their position of power and authority.[61]

1.5 Assumptions of the Research

The research assumes that legal and regulatory restraints on excessive executive director powers and remuneration are necessary but not adequate or exhaustive for the effective and efficient running of companies from the perspective of good corporate governance. It also assumes that good corporate governance is essential for the overall success of a country and its businesses. The research further assumes that forceful imposition of corporate governance rules is unlikely to be effective unless directors voluntarily adhere to them.

1.6 The Framework of the Dissertation

The remainder of the dissertation is organised into chapters as outlined below.

In Chapter 2, the theoretical framework regarding the duties and powers of directors, largely in a common law context and with reference to the South African statutes, is discussed. In an environment in which governments and the courts are becoming

---

[59] Rossouw G. J, Van der Watt A, Malan D. P, Corporate Governance in South Africa, (2002) *Journal of Business Ethics*, 37, 289–302.

[60] Terry Booysen, *The Case For Good Governance - Past, Present And Future,* CGF Research Institute, 14 May 2009, available at www.cgfresearchinstitute.com/LinkClick.aspx?fileticket (visited on 18 July 2009).

[61] Horn R F, *The Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 15-17.

المنارة للاستشارات
www.manaraa.com

increasingly vigilant in prosecuting and disciplining directors for failing to fulfill their duties, it is important to understand what is expected of the directors when conducting company business especially considering their relevance in achieving good corporate governance. The discussion on directors' duties is therefore, important in that it highlights the need for directors to know and observe their common law and statutory duties as one of the tools to achieve good corporate governance.

After a general discussion of directors' duties, the corporate governance framework that South African legislatures and committees have put in place to regulate directors' conduct and ensure good corporate governance is discussed. In this regard particular reference is made to the major corporate governance related legal and regulatory provisions relating to directors' powers and remuneration. The *King Codes*, Companies Act (Act 61 of 1973 and Act 71 of 2008) and the *Johannesburg Securities Exchange (JSE) Listings Requirements* are discussed to understand how they deal with the powers and remuneration of directors as some of the key aspects of corporate governance. The research is based on legislation and regulations in place as at 31 July 2010.

In Chapter 3 an analysis and evaluation of the South African legal and regulatory restraints on executive director powers and excessive remuneration, discussed in chapter 2, is done. The main objective of analysing the reports and legislation is to assess whether they provide sufficient limits on directors' powers and their remuneration to achieve good corporate governance. The limitations of the legal and regulatory aspects of corporate governance regarding directors' powers and remuneration in enhancing corporate governance are also examined.

In Chapter 4, given the comparative value of South Africa and United Kingdom legal systems, a comparison of the two countries' corporate governance laws and regulations in relation to directors' powers and remuneration is undertaken. In this chapter, the main objective is to establish how South Africa has performed with regards to corporate governance laws and regulations compared to other countries especially developed

المنارة للاستشارات
www.manaraa.com

countries. Like the previous chapters, the comparison will mostly focus on directors' powers and remuneration aspects of corporate governance.

In Chapter 6, a summary and conclusion of the research is prepared. Recommendations also constitute part of this chapter.

1.7 Research Methods

The research involves a literature study of books, electronic/internet sources, journal articles, theses and dissertations, decided cases and legislation. The study is principally an analysis and evaluation of the literature relevant to legal and regulatory restraints on powers and excessive remuneration of executive directors in South Africa. The analysis is done from the perspective of corporate governance.

1.8 Reference Techniques

For the purpose of this research, company directors are referred to in the masculine form. Sources of reference are cited in full when first quoted and thereafter in abbreviated form in the footnotes. Full references are shown in the bibliography at the end of the dissertation.

المنارة للاستشارات
www.manaraa.com

CHAPTER 2

CORPORATE GOVERNANCE IN SOUTH AFRICA

2.1 Duties and Powers of Directors

2.1.1 Introduction

The increased focus on good corporate governance has led to a renewed interest in the duties of company directors.[62] One cannot appreciate the importance of the legal and regulatory measures on directors' powers and remuneration if one does not understand the powers vested in the directors and duties expected of them in the running of companies.[63] This chapter therefore, explains the various duties of directors and their powers so that when the corporate governance legal and regulatory mechanisms are discussed the objective which they seek to achieve can be easily appreciated.

Historically, directors' duties in South Africa and many other jurisdictions were owed almost exclusively to the company and its members, and the board was expected to exercise its powers for the financial benefit of the company.[64] However, more recently there have been attempts to lighten the position, and provide for more scope for directors to act as good corporate citizens by considering a wide range of other stakeholders'

---

[62] Van Der Linde K, The Personal Liability of Directors for Corporate Fault –An Exploration, (2008) 20 *South African Mercantile Law Journal* 439–461. Scandals and corporate collapses such as Enron, Parmalat, Saambou and Fidentia have also brought the duties and responsibilities of directors into the spotlight.

[63] The day to day running of the company is not the responsibility of shareholders but is that of directors, particularly executive directors who are responsible for the day to day management of the company and for ensuring that the company observes good corporate governance. (Colley Jr., J L; Doyle J L; Logan G W. & Stettinius W, *Corporate Governance*, (New York: McGraw-Hill 2003) 3-5).

[64] Havenga M K, Directors' Fiduciary Duties under our Future Company Law Regime, (1997) 9 *South African Mercantile Law Journal* 310- 324.

المنارة للاستشارات
www.manaraa.com

interests.[65] Directors have to realise that they do not act independently but that their actions and decisions impact on the societies and environments in which they operate.[66] They should thus, whilst seeking to maximise profit for the company, exercise their duties in the best interests of the company and all other stakeholders.[67] This represents a considerable departure from the traditional notion that directors' duties are owed only to the company being the shareholders collectively. It is therefore ultimately the responsibility of the directors to maintain good relationships with all stakeholders and to ensure good corporate governance.[68]

The duties imposed upon directors are fiduciary duties, similar in nature to those that the law imposes on those in similar positions of trust, for example agents and trustees.[69] Since directors exercise control and management over the company for the benefit of the shareholders and other stakeholders, the law imposes strict duties on the directors in relation to the exercise of their duties. In practice, the amount of power exercised by and the legal responsibilities of directors vary with the nature of the organization, and with the jurisdiction within which they operate.[70] Although directors are entrusted with the power to manage a company, their power to do so is not unrestrained as they are obliged

---

[65] Chapter 8 of the *King III.* See also Esser I, *Recognition of Various Stakeholder Interests in Company Management*, Published LLD Thesis, (UNISA 2008) 211-213. Specific legislation makes it mandatory for companies to consider the interests of certain stakeholders for example, the Labour Relations Act 66 of 1995 and the Promotion of Access to Information Act 2 of 2000.

[66] Institute of Directors in Southern Africa, *Executive Summary of the King Report* 2002, available at www.iodsa.co.za (visited on 12 August 2009).

[67] South Africa recognises, at common law, the doctrine of enlightened shareholder value vs the pluralist approach, in terms of which directors are entitled to take cognisance of the interests of all stakeholders of a company including employees, the community, the environment, consumers and so forth (see chapter 4 paragraph 4.2 for a detailed discussion on the issue). See Esser I & Dekker A, The Dynamics of Corporate Governance in South Africa: Broad Based Black Economic Empowerment and the Enhancement of Good Corporate Governance Principles, (2008) *Journal of International Commercial Law and Technology*, Vol. 3(3) 157-169.

[68] Commonwealth Association for Corporate Governance. *CACG Guidelines: Principles for Corporate Governance in the Commonwealth*, (1999), available at http://www.ecgi.org/codes/code.php?code_id=24 (visited on 15 August 2009). See also comments from Mervyn King in *Governance for all Entities*, where he states that "Directors in the twenty-first century have to be seen to be directing companies to be good corporate citizens. The inclusive approach recognizes that a company is a link that brings together the various stakeholders relevant to the business of the company." (King M, *Governance for all Entities,* The Corporate Citizen, (Johannesburg 2006) 14).

[69] Esser I, *Recognition of Various Stakeholder Interests in Company Management*, (2008) 206-210.

[70] Davies P. L, *Gower's Principles of Company Law*, 6th Edition (London: Sweet & Maxwell 1997) 1-5.

المنارة للاستشارات
www.manaraa.com

to act both within the powers of the company and within their fiduciary duties to the company.[71]

As Hahlo said, the ‘‘paramount duty of directors, individually and collectively, is to exercise their powers *bona fide* in the best interests of the company.’’[72] The various duties to which company directors are subjected to include common law[73] and statutory[74] duties, as well as those derived from the company's Memorandum of Incorporation.[75] Directors' duties are categorised into fiduciary duties of good faith and the duty to act with the necessary care and skill when performing company duties.[76] These duties are discussed below.

2.1.2 Duty to Act in Good Faith

Directors must act honestly, in good faith (*bona fide*) and in the best interests of the company.[77] Directors' fiduciary duties of good faith include the duty to prevent a conflict of interests, not exceed the limitation of their power, maintain an unfettered discretion and exercise their powers for the purpose for which they were conferred.[78]

---

[71] Section 76 of the Companies Act 71 of 2008 and Chapter 2 of the *King III*.

[72] Pretorius J T, Delport P A, Havenga M and Vermas M, Hahlo's *South African Company Law Through the Cases*, 6th Edition, (Juta & Co, Kenwyn 1999) 279.

[73] Naidoo defines common law as "a law which is not legislated in the statute books of a country, but which nevertheless over time and through wide acceptance gains the force of a law." (Naidoo R, *Essentials for Corporate Governance for South African Companies,* (Cape Town: Double Storey 2002) 11).

[74] See Esser I and Coetzee J, Codification of Directors' Duties, (2004) 12 *Juta's Business Law*, 26-31. The Companies Act is the main Act (for example sections 234–251 of Companies Act 61 of 1973 and section 75-77 of Companies Act 71 of 2008) with other legislation also providing for directors' duties for example the Labour Relations Act (1995) and the Income Tax Act (1997).

[75] Van Dorsten C, *The Law of Company Directors in South Africa* (Meridian Press CC 1999). See also *Cyberscene Ltd v i-Kiosk Internet and Information (Pty) Ltd* 2000 (3) SA 806 (C) 813–814 where the directors' fiduciary duties have also been confirmed and where the court held that a director stands in a fiduciary relationship to the company from the moment he begins to act as a director, even if he has not been formally appointed.

[76] *Re City Equitable Fire Insurance Co Ltd* [1925] Ch 407.

[77] Cilliers H S, Benade M L, Henning J J, Du Plessis J J, Delport P A, De Koker L, Pretorius JT, *Corporate Law*, 3rd Edition, (Butterworths, Durban 2000) 141.

[78] Ibid.

المنارة للاستشارات
www.manaraa.com

2.1.2.1 Conflict of Interest

2.1.2.1.1 Common Law

As fiduciaries, the directors may not put themselves in a position where their interests and duties conflict with the duties that they owe to the company.[79] By definition, where a director enters into a transaction with a company, there is a conflict between the director's interest (to do well for himself out of the transaction) and his duty to the company (to ensure that the company gets as much as it can out of the transaction).[80] This rule is so strictly enforced that, even where the conflict of interest or conflict of duty is purely hypothetical, the directors can be forced to disgorge all personal gains arising from it.[81] "The law's position is that good faith must not only be done, but must be seen to be actually done, and seriously monitors the conduct of directors in this regard; and will not allow directors to escape liability by contending that his decision was in fact well founded."[82]

Traditionally, the law has divided conflicts of duty and interest into two categories, namely the corporate opportunity rule and the no-profit rule.[83] The corporate opportunity

---

[79] See *Phillips v Fieldstone Africa (Pty) Ltd,* 2004 (3) SA 465 (SCA), a case in which the Supreme Court of appeal dealt with the fiduciary duty an employee owes an employer and concluded that as Phillips (the employee) stood in a fiduciary relationship to Fieldstone (the employer) when the opportunity became available to him it did not belong to him, but to Fieldstone. Another case is *Robinson v Randfontein Estates Gold Mining Company Limited* 1921 (AD) 168 where it was held that "where one man stands to another in a position of confidence involving the 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 interests conflict with his duty". See also Pretorius J T, *et al*, Hahlo's *South African Company Law Through the Cases*, (1999) 305-309.

[80] Davies P. L, *Gower's Principles of Company Law*, (1997) 141-153.

[81] See *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168**,** where a director of the plaintiff company had purchased property in circumstances under which it was his duty to acquire the property for the company and not for himself. The court ruled that a director will not be allowed to retain a benefit or profit obtained through a breach of his fiduciary duties to the company.

[82] Adler A, *Type of Director Duties Based On Enron Case From The Perspective Company Law In Malaysia*, available at http://www.scribd.com/Type-Of-Director-Duties-Based-On-Enron-Case/d/14179407 (visited on 10 January 2010).

[83] Maleka F C, Da Silva v C H Chemicals (Pty) Ltd: Fiduciary Duties of Resigning Directors, (2009) *SALJ* Vol. 126(1) 61-70.

المنارة للاستشارات
www.manaraa.com

rule prohibits a director from appropriating for himself or for another property or economic opportunities which either belong to the company or to which the company has some kind of claim,[84] so that the acquisition of the opportunity by the director would take place at the expense of the company.[85] A director is thus regarded as a trustee of company property and is not expected to knowingly participate in or ignore the misuse of company property and to, without the informed consent of the company, use for his own profit the company's assets, opportunities, or information.[86] Where he acts in breach of this duty he will be liable for any profits he makes or for damages in respect of any loss the company may have suffered as a result of his actions.[87]

In contrast, the no-profit rule is breached where a director makes a profit which may consist not only of money but also any other gain or advantage as a result of his office even though the acquisition by the director was done in good faith and is not at the expense of the company.[88] In *Regal (Hastings) v Gulliver*[89] the House of Lords, in upholding what was regarded as a wholly unmeritorious claim by the shareholders, held that:

> "*(i) what the directors did was so related to the affairs of the company that it can properly be said to have been done in the course of their management and in the utilisation of their opportunities and special knowledge as directors; and (ii) that what they did resulted in profit to themselves*."

Accordingly, the directors were required to give back the profits that they made, and the shareholders received their windfall.[90]

---

[84] See Beuthin R C & Luiz S M, *Beuthin's Basic Company Law,* 3rd Edition (2000) 198-199, where it was said generally the company has "some kind of claim" where the opportunity falls within the line of business of the company and the company is justifiably relying on the director to acquire the opportunity for it.

[85] Beuthin R C, Corporate Opportunities and the No-profit Rule, (1978) 95 *SALJ*, 458-462.

[86] Sher H, *Company Directors' Duties and Responsibilities*, (2005) Juta's Business Law Vol 13(3) 129-131.

[87] Campbell D & Woodley S, *Trends and Developments in Corporate Governance*, (Kluwer Law International 2003) 19-20.

[88] *Regal (Hastings) Ltd v Gulliver* [1942] All ER 378.

[89] Ibid.

[90] See also *Symington v Pretoria-Oos Privaat Hospitaal Bedryfs (Pty) Ltd* 2005 (5) SA 550 (SCA).

المنارة للاستشارات
www.manaraa.com

From the above, it is apparent that it is almost impossible for directors to compete directly with the company without a conflict of interests arising. Similarly, they may not act as directors of competing companies,[91] as their duties to each company would then conflict with each other. A director may obtain no other advantage from his position as a director than that to which he is entitled by way of remuneration.[92] The determining factor is whether or not the benefit was obtained as a result of the director's office and not whether the director acted in good or bad faith.[93] It is also worth noting that, a director must take care to avoid breaching both categories (the corporate opportunity rule and the no-profit rule) of this fiduciary duty to avoid a conflict of interest.[94] If the director fails to make the required disclosure the contract is voidable against him at the instance of the company.[95] The object of the rule is to prevent directors from placing themselves in a position where they may be tempted to prefer their own interests at the expense of the company.

2.1.2.1.2 Companies Act 61 of 1973

In terms of sections 234-241 of Companies Act 61 of 1973, a director has to inform his company of any personal financial interests he may have in a contract which has been or

[91] *Sibex Construction (SA) (Pty) Ltd v Injectaseal CC* 1988 (2) SA 54 (T). This case dealt with directors who formed a close corporation in competition with the company of which they were directors and the court held that the unauthorized use of confidential information was a breach of the directors' fiduciary duties and that the directors remained under a fiduciary obligation even after their resignations.

[92] See *Magnus Diamond Mining Syndicate v Macdonald and Hawthorne* 1909 ORC 65, where directors were ordered to transfer land back to the company and account for profits obtained from diamondiferous land purchased in competition with their company.

[93] See *Du Plessis v Phelps* 1995 4 SA 165 (C) 171 where it was held that "liability for a breach by a director of his fiduciary duties does not necessarily involve *dolus or culpa"*.

[94] See *Da Silva & others v C H Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA) where it was held that when a director is in breach of his duty the company may claim the opportunity from the director or, where such a claim is no longer possible, it may claim any profits which the director may have made as a result of the acquisition of the opportunity or it may claim damages in respect of any loss which it may have suffered. See also Maleka FC, Da Silva v C H Chemicals (Pty) Ltd: Fiduciary Duties of Resigning Directors, (2009) 61-70.

[95] See *African Claim and Land Co. Ltd v W J Langermann,* 1905 TS 494 where it was held that "a director is in a fiduciary duty towards the company in carrying on its affairs and it is a breach of duty on his part to stand by and allow his co-directors to enter into a contract in which he has a personal interest without disclosing that interest to them. A contract so entered can be rescinded by the company after it has acquired knowledge of the facts".

المنارة للاستشارات
www.manaraa.com

is to be entered into by the company, whether directly or indirectly, in advance or immediately after acquiring the interest and the company must maintain a register of such interests. To ensure that directors comply with this requirement, any director or officer of a company who fails to comply with any of the provisions regarding declaration of interest is guilty of an offence.[96]

2.1.2.1.3 Companies Act 71 of 2008

This duty is also specifically provided for in the Companies Act 71 of 2008 which proposes to enhance corporate accountability and to ensure that directors are aware of their duties and responsibilities by partially codifying directors' duties[97] and specifically setting a standard of directors' conduct.[98] In terms of section 76(3) of the Companies Act 71 of 2008, directors must exercise the powers and perform the functions of director honestly and in good faith (*bona fide*) and for a proper purpose.[99] As fiduciaries, the directors may not put themselves in a position where their interests and duties conflict with the duties that they owe to the company.[100] If a director makes a personal profit from a transaction by virtue of his position as a director, he or she must account to the company for the profit made, unless he or she had already disclosed all the facts to the shareholders in a general meeting and obtained their approval of the transaction.[101]

---

[96] See section 237(5) of the Companies Act 61 of 1973.

[97] See a more detailed discussion on codification in paragraph 2.2.3.2 below. It should however, be noted that section 76(6) of the Act provides for partial codification of directors' duties in that the provisions of the section are in addition to, and not in substitution for, any duties of the director of a company under the common law which means that directors would still be obliged to comply with their common law duties as long as they are not expressly amended or in conflict with the section (Davies D *et al, Companies and Other Business Structures in South Africa*, (Oxford University Press Southern Africa (Pty) Ltd 2009) 102-103) .

[98] Section 76 of the Companies Act 71 of 2008.

[99] Section76(3) provides that, "a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director—
(a) in good faith and for a proper purpose;
(b) in the best interests of the company;"

[100] See section 76(2) of the Companies Act 71 of 2008 which prohibits a director of a company from using his position or any information obtained while acting in the position to gain an advantage for himself or for another person other than the company or a wholly-owned subsidiary of the company. See also Havenga M, Directors in Competition with Their Companies, (2004) *South African Mercantile Law Journal* 275.

[101] Section 75 of the Companies Act 71 of 2008. See also Cilliers *et al*, *Corporate Law*, (2000) 141-144.

المنارة للاستشارات
www.manaraa.com

In terms of section 75 of the Companies Act 71 of 2008, a director has to inform the board or shareholders in certain circumstances, of any personal financial interests he may have in a contract which has been or is to be entered into by the company, whether directly or indirectly, in advance or immediately after acquiring the interest and the company must maintain a register of such interests.[102] The director is obliged to declare the nature and extent of that interest to the Board or shareholders depending on the situation and the material circumstances relating to the director or related person's acquisition of that interest.[103] He also must not take part in the consideration of the matter, except in exceptional circumstances.[104]

The main idea behind the provisions is to limit directors' powers to enter into contracts with companies where conflicts of interest may arise as well as to enhance transparency and independence. The possible danger is that the director may be driven by the desire to give business to companies where they will also benefit at the expense of the company they are working for. As an enforcement measure, the Act provides for liability of directors where they have acted outside the authority vested in them and when their actions were contrary to the provisions of the Act.[105]

---

[102] While a director must still disclose any conflict of interest he has in relation to a matter before the board (as was previously the case), the concept of a conflict of interest is extended to include a personal financial interest of a person related to the director. In terms of section 75(7) a decision by the board, or a transaction or agreement approved by the board, or by a company is valid despite any personal financial interest of a director or person related to the director, if it was approved in the manner contemplated in the section or has been ratified by an ordinary resolution of the shareholders.

[103] Section 75 of the Companies Act 71 of 2008. If the director does not declare the interest as required, a court, upon application by an interested person, may declare valid a transaction that has been approved by the Board, despite the director's failure to satisfy the disclosure requirements. However, according to Delport, the fact that the Companies Act 71 of 2008 does not exclude the common law principle that all contracts between a director and the company are voidable at the instance of the company means that the principle will continue to apply in certain circumstances. (Delport P, *The New Companies Act Manual*, (LexisNexis 2009) 60-62).

[104] Section 75 of the Companies Act 71 of 2008. However, it is important to note that, a director is not obliged to disclose personal interests in certain circumstances, for example, if he holds all the beneficial interests of all the issued securities of the company and is the only director of that company (section75).

[105] See section 77(2) of the Companies Act 71 of 2008 which provides that, a director of a company may be held liable in compliance with the principles of the common law relating to breach of a fiduciary duty or delict for any loss, damages or costs sustained by the company as a consequence of any breach by the director of a duty contemplated in any provision of the Act or any provision of the company's Memorandum of Incorporation.

المنارة للاستشارات
www.manaraa.com

2.1.2.1.4 The Johannesburg Securities Exchange Listings Requirements

To promote transparency, independence and accountability, the L*istings Requirements* provide for declaration of directors' interests. Companies seeking a listing must submit to the JSE a director's declaration for each director, evidencing that the directors are free of conflicts of interest between the duties they owe the company and their private interests.[106] This is aimed at ensuring that directors do not, without the informed consent of the company, use the company's assets, opportunities, or information for their own profit.

2.1.2.2 Duty Not to Exceed the Limitation of Their Power

The major concern of corporate governance has been the extent to which directors exercise their powers in the interests of shareholders and other stakeholders in the company and whether such powers should be restricted.[107] Generally directors must manage the company within the limits of company law, other legislation, the Memorandum of Incorporation,[108] common law and any directions given through special resolutions by shareholders voting in company general meetings.[109]

2.1.2.2.1 Common Law and Companies Act of 61 of 1973

In terms of the 1973 Act, directors were supposed to derive their powers from common law, the Act itself and the Memorandum and Articles of Association.[110] However, in

---

[106] Sections 3 & 4 of *JSE Listing Requirements*.

[107] Coyle B, *Corporate Governance*, (2003) 44-61.

[108] This was referred to as the Memorandum and Articles of Association in Act 61 of 1973.

[109] Cilliers *et al*, *Corporate Law*, (2000) 141-144.

[110] The Memorandum of Association determined the scope of the company's objects and powers, while the articles of association were internal rules by which a company was governed which was sometimes defined as a contract between members themselves and between members and the company (Pretorius J T, *et al*, Hahlo's *South African Company Law Through the Cases*, (1999)) 341-344).

المنارة للاستشارات
www.manaraa.com

certain instances an individual director may still bind the company by his acts by virtue of his ostensible authority.[111] Although directors have powers to bind the company to legal transactions, these powers are subjected to some legal and regulatory restrains as a way of ensuring that the interests of shareholders and other stakeholders are sufficiently satisfied.[112] The articles, for instance, may sometimes seek to limit these powers or to specify particular duties, in which event these limitations must be strictly complied with. A director may, therefore, not engage in transactions on behalf of the company which are beyond the powers conferred upon him by the articles, legislation and other regulatory authorities.[113]

Another example is that directors may not exercise or delegate any powers of the company which are required to be exercised by the company in a general meeting in terms of the Companies Act.[114] However, it is important to note that if certain matters are assigned to the board of directors in terms of the articles of association, then only the board has the power to deal with those matters.[115] The general meeting may, however, intervene with the powers of the board in certain matters. These matters include situations where the board of directors refuses or is unable to institute action on behalf of

[111] See the rule in *Royal British Bank v Turquand* (1856) 6 E&B 327 which states that a third party dealing with a company is entitled to presume that a person held out by the company has the necessary authority to act on behalf of the company.

[112] Section 86 of Act 61 of 1973. See also Coyle B, *Corporate Governance*, (2003) 44-51.

[113] However, it is important to note that in terms of section 36 of Act 61 of 1973 no act of a company shall be void because the directors had no authority to perform that act on behalf of the company by reason only of that fact and, except in certain special circumstances. See also Grant Thornton South Africa, *Directors' Duties, Responsibilities and Rights,* available at: http://www.gt.co.za/Publications/Effective-directors-guide/directors_duties.asp (visited on 17 November 2009).

[114] See for example section 221 of the Companies Act 71 of 2008 which restricts powers of directors to issue share capital. See also Van der Merwe J G, Appleton R B, Delport P A, Furney R N, Mahony D P, Koen M, *South African Corporate Business Administration*, (2009) 15.1-15.32.

[115] See *Automatic Self-Cleansing Filter Syndicate Co v Cunningham* [1906] 2 Ch 34 where it was held that the division of powers between the board and the shareholders in general meeting depended upon the construction of the articles of association and that, where the powers of management were vested in the board, the general meeting could not interfere with their lawful exercise.

المنارة للاستشارات
www.manaraa.com

the company or when certain powers have been reserved for the board of directors, but the particular act is voidable because the board has exceeded or abused its powers.[116]

2.1.2.2.2 Companies Act 71 of 2008

Although the directors' duties in South Africa have been largely regulated by the common law, in a change of approach, the Companies Act 71 of 2008 has preserved the common law duties by partially codifying[117] these duties through the introduction of a number of provisions relating to the standards of conduct of directors.[118] The Companies Act 71 of 2008 proposes to enhance corporate accountability and to ensure that directors are aware of their duties and responsibilities by codifying director's duties and specifically sets a standard of director's conduct.[119] It should, however, be noted that section 76(6) of the Act provides that the provisions of the section are in addition to, and not in substitution for, any duties of the director of a company under the common law. This means that directors would still be obliged to comply with their common law duties unless the duties are specifically amended by section 76 or are in conflict with the section.[120] However, in terms of section 218 "nothing in this Act renders void an agreement, resolution or provision of an agreement, resolution, Memorandum of Incorporation or rules of a company that is prohibited, void, voidable or may be declared unlawful in terms of this Act, unless a court declares that agreement, resolution or provision to be void."

---

[116] See *Shaw & Sons (Salford) Ltd v Shaw* [1935] 2 KB 113 where it was held that the only way in which the general body of the shareholders can control the exercise of the powers vested by the articles in the directors is by altering their articles, or, if the opportunity arises under the articles, by refusing to re-elect the directors of whose actions they disapprove.

[117] Partial codification of directors' duties means that the Act will not replace the common law duties of directors that are not expressly amended or are not in conflict with the Act (Delport P, *The New Companies Act Manual*, (2009) 58-59).

[118] See section 76 of the Companies Act 71 of 2008.

[119] Ibid.

[120] See section 76 which specifically provides for the continued applicability of common law.

المنارة للاستشارات
www.manaraa.com

Similar to the 1973 Act, most decision making powers in a company are held by the board of directors "which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that Act or the company's Memorandum of Incorporation provides otherwise."[121] The exercise by the directors of their powers usually occurs in meetings and the powers are given to them as a whole and not to individual directors although delegation to a committee consisting of one or more directors is acceptable.[122]

In terms of the Companies Act 71 of 2008, the Memorandum of Incorporation and any rules of the company are binding between the company and each director or prescribed officer of the company in the exercise of their respective functions within the company.[123] Whilst the Memorandum of Incorporation seeks to limit or restrict the powers or activities of directors it is important to note that the company is precluded from denying responsibility for the directors actions merely because the Memorandum of Incorporation limits, restricts or qualifies the purposes, powers or activities of that company or as a consequence of that limitation, restriction or qualification, the directors had no authority to authorise the action by the company.[124] However, in South Africa, like in many jurisdictions, the members of the company are permitted to ratify transactions which would otherwise fall foul of the good faith principle provided the director's action does not contravene the Act.[125]

---

[121] Section 66 of the Companies Act 71 of 2008. See also Pretorius *et al*, *Hahlo's South African Company Law through the Cases*, (1999) 341-344.

[122] Section 72 of the Companies Act 71 of 2008.

[123] Section 15 of the Companies Act 71 of 2008. It is important to note that the Memorandum of Incorporation must be consistent with the provisions of the Act and any provision that is inconsistent with the provisions of the Act will be regarded as void to the extent that it contravenes or is inconsistent with the Act.

[124] Section 20 of the Companies Act 71 of 2008. A third party who obtained rights in good faith and did not have knowledge of the limitation, restriction or qualification retains the "rights" under the contract whereas the one who acted *mala fide* will not have any "rights" under the contract. Also if there is lack of authority on any other basis which is not the limitation, restriction or qualification on the capacity of the company, the company is not bound by the contract even if the third party acted in good faith. However, Delport argues in his book, *The Companies Act Manual*, that it is uncertain how the innocent party will obtain "rights" if the action is restrained for example before the contract is concluded. (Delport P, *The New Companies Act Manual*, (2009) 38-39).

[125] Section 20 of the Companies Act 71 of 2008. According to Delport the shareholders may ratify any action that is inconsistent with the limits, restrictions or qualifications provided in the Memorandum of Incorporation as long as it does not contravene the Act. He further indicates that in terms of section 20(5) shareholders may even ratify fraudulent actions by special resolution. (Delport P, *The New Companies Act Manual*, (2009) 38-39).

المنارة للاستشارات
www.manaraa.com

Directors may be liable to the company for any financial losses incurred by it as a result of them having acted outside the scope of their authority.[126] Any member of the company may institute action against any incumbent or previous director who "fraudulently or due to gross negligence causes the company to do anything inconsistent with a limit, restriction or qualification unless the fraudulent act or gross negligence has been ratified by the shareholders."[127]

2.1.2.3 Unfettered Discretion and Proper Purpose

2.1.2.3.1 Common Law

Directors cannot, without the consent of the company, fetter their discretion in relation to the exercise of their powers, and cannot bind themselves to vote in a particular way at future board meetings.[128] This principle is applied even if there is no improper motive or purpose, and no personal advantage accrues to the director. A director must also not allow his judgment to be interfered with and must objectively apply his mind to the business of the company.[129] Where he is appointed to represent certain shareholders he is still obliged to exercise his discretion and must act positively to protect the interests of the company even if they conflict with those of the people who elected him.[130]

---

[126] Section 77 of the Companies Act 71 of 2008.

[127] See section 165 of the Companies Act 71 of 2008 respectively, which provide for initiation of proceedings on behalf of company by a member. See also Delport P, *The New Companies Act Manual*, (2009) 38-39.

[128] Ferran E, The Decision of the House of Lords in Russel v Northern Bank Development Corporation Ltd, (1994) *Cambridge Law Journal*, Vol. 53(2) 343-366.

[129] Campbell D & Woodley S, *Trends and Developments in Corporate Governance,* (2003) 17-18.

[130] See *Fisheries Development Corporation of SA Ltd v Jorgensen & Another; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd & Others* (1980 (4) SA 156 (W) at 156) where it was held that "……in carrying out his duties and functions as director, he is in law obliged to serve the interests of the company to the exclusion of any such nominator, employer or principal".

المنارة للاستشارات
www.manaraa.com

Directors must exercise their powers for a proper purpose which means that they should exercise their powers only for the purpose for which they are conferred.[131] Two duties may be distinguished with regards to purpose, the first being the duty to exercise their powers in good faith in the interests of the company and the second being the duty not to exercise powers for an unauthorised or collateral purpose. Directors should thus use their powers for the company's benefit and not for their own gain and should act within the confines of the company's Memorandum of Incorporation and all relevant legislation.[132] Difficulties arise where the director, while acting in good faith, is serving a purpose that is not regarded by the law as proper.[133] In such cases directors become liable even where they acted honestly and the court can set aside the improper purpose.[134]

2.1.2.3.2 The Companies Act

The Companies Act 61 of 1973 does not specifically refer to the director's duty to act in good faith and for a proper purpose and common law has been used to establish whether one acted in good faith and for a proper purpose. In a change of approach, the Companies Act 71 of 2008 specifically requires a director to exercise the powers and perform the functions of director in good faith and for a proper purpose.[135] Like under common law, directors must therefore exercise their powers only for the purpose for which they are conferred.[136]

---

[131] Section 76 of Companies Act 71 of 2008. See also Cilliers *et al*, *Corporate Law,* (2000) 141-142.

[132] Campbell D & Woodley S, *Trends and Developments in Corporate Governance,* (2003) 16-17.

[133] One of the leading authorities in relation to what amounts to a proper purpose is the Privy Council decision of *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 832. The case concerned the power of the directors to issue new shares. It was alleged that the directors had issued a large number of new shares purely to deprive a particular shareholder of his voting majority. The Privy Council held that the board had acted for an improper purpose although they had acted honestly and not in their self interest. See also *Hogg v Cramphorn Ltd* [1967] Ch. 254 where directors fearing a takeover bid and their subsequent removal from the board of directors they allotted shares to their supporters. The court held that although the directors acted under the belief that it would be in the company's interests to preserve their board positions they had acted for an improper cause and thus declared the allotment of the shares to be voidable.

[134] Farrar J H & Hannigan B M, *Farrar's Company law*, 4th Edition (Butterworths 1998) 380-384.

[135] Section 76(3) of the Companies Act 71 of 2008.

[136] Where a director exceeds the power conferred on him his actions can only be validated through ratification by shareholders (section 20 of the Companies Act 71 of 2008).

المنارة للاستشارات
www.manaraa.com

2.1.3 Duty of Care, Skill and Diligence

2.1.3.1 Common Law

In contrast to directors' onerous duties of good faith and loyalty, the common law historically expected very little of directors in terms of the standard of care and skill.[137] Some authors argue that the common law gave directors the freedom to manage companies incompetently.[138]

In South African law, the paramount duty of a director is to observe the utmost good faith towards the company and to undertake all actions and decisions to the benefit of the company. In discharging that duty, a director must act with the necessary care and skill. The South African position was summarised by Margo J[139] in three broad propositions that draw on earlier English decisions.[140] The first proposition is that 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 other particular obligation assumed by or assigned to the specific director. The degree of care required is different for executive and non-executive directors.[141] The non-executive director need not give continuous attention to the affairs of the company as his duty of care is sporadic, has to be performed at periodic board meetings and at any other meetings that may require his attention.[142] He is not obliged to attend all such meetings, though he ought to do so whenever he reasonably

---

[137] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, *(*2008) 97.

[138] See Finch V, *Company Directors: Who Cares about Skill and Care?,* 55 *Modern LR179* at 179 (1992) and also *Turquand v Marshall* ([1869] LR 4 App 376 (Ch D)) and Re *National Bank of Wales Ltd* ([1899] 2 Ch 629 (CA)), cases which confirmed that directors cannot be held liable unless they act grossly negligently.

[139] *Fisheries Development Corporation of SA Ltd v Jorgensen & Another; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd & Others* (1980) (4) SA 156 (W) at 156.

[140] Examples of the earlier decisions which confirm the propositions are *Re Brazilian Rubber Plantations and Estates Ltd* (1911) 1 Ch 425 and *Re City Equitable Fire Insurance Co* [1925] Ch 407 at 429.

[141] *Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd & others* 1980 (4) SA 156 (W) at 165F-166D.

[142] *Re City Equitable Fire Insurance Co* [1925] Ch 407 at 429.

المنارة للاستشارات
www.manaraa.com

can. By contrast, an executive director participates in the day-to-day management of the company's affairs, or part of it, and his employment contract usually stipulates that he must devote his full attention to the company business.[143]

Secondly a director is not required to have any special business acumen or expertise, ability or intelligence, or even expertise in the company business.[144] In this regard Romer J[145] found that a director is required to use the degree of care which an ordinary man might be expected to take in the circumstances and need also not exhibit in the performance of his duties a greater degree of care and skill than may reasonably be expected from a person of his knowledge and experience.[146] Under this proposition, a director's skills will be judged subjectively and the courts will take the directors personal qualifications and expertise into consideration.[147] In other words, if a director has any special expertise, he is expected to give the company the benefit of it. A higher standard will thus be applied when the director has been appointed as an expert and possesses technical knowledge or professional skills.[148] Although a director is not expected to possess special expertise, he becomes liable for delict in damages or for breach of contract (if there is a contract between him and the company) if he does not act with the care and skill that may reasonably be expected from a person of his knowledge, skill and

---

[143] Ibid.

[144] See *Re Brazilian Rubber Plantations & Estates Ltd* [1911] 1 Ch 425 at 437 which contains the dictum: "He [i.e. the director] is, I think, not bound to bring any special qualifications to his office. He may undertake the management of a rubber company in complete ignorance of everything connected with rubber, without incurring any responsibility for the mistakes that may have been caused by his ignorance ....".

[145] *Re City Equitable Fire Insurance Co* [1925] Ch 407 at 427-429.

[146] See also *Re Brazilian Rubber Plantations and Estates Ltd* (1911) 1 Ch 425 at 437 where it was held that, when performing their duties, directors must attend carefully to the affairs of the company and must exhibit the "reasonable care" which any ordinary person might be expected to take under the same circumstances.

[147] Mervyn King, on the relationship between the company and its directors, states that: "While the board has collective authority, each director has individual responsibility. Consequently, if a decision of the board subsequently turns out to have been a bad business judgment call and it is contended that this amounts to a failure in the duty of care, the law looks at the conduct of each director and his level of experience in deciding whether or not that director is responsible." (Mervyn King, *Governance for all entities,* (2006) 36).

[148] See *Henway Freight Services (Pty) Ltd v Grogor* 2007 (2) SA 561 (SCA) at 564D-E where the Court held that that regard should be had to any additional knowledge, experience or qualifications that the evidence reveals that the director possessed.

المنارة للاستشارات
www.manaraa.com

experience.[149] He, however, is not liable for mere errors of judgment. 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.

Thirdly, where a director assigns duties to some official, he is, in the absence of suspicion, justified in trusting that official to perform such duties honestly. Likewise, unless proper reasons exist for querying such, a director is also entitled to rely on the judgment, information and advice of the management.[150] However, a director exercising reasonable care would not accept information and advice without giving it appropriate consideration and applying his own mind accordingly. Each director must therefore, based on personal knowledge and experience as well as the information and advice given by company officials, try to understand the company business and affairs so as to be able to make informed decisions.[151]

Despite the above, it is important to note that a more modern approach has since developed, and in *Dorchester Finance Co Ltd v Stebbing* [1989] BCLC 498 the court held that the rule in *Equitable Fire* related only to skill, and not to diligence. With respect to diligence, what was required was:

> *"such care as an ordinary man might be expected to take on his own behalf"*

More recently, it has been suggested that both the tests of skill and diligence should be assessed objectively and subjectively. On the other hand the existence of contracts of service between directors and companies appears to have caused a departure from the traditional subjective approach in *Re City Equitable Fire Insurance Co Ltd* because in terms of such a contract of service, a director would be required to display an objective

[149] Cilliers *et al*, *Corporate Law,* (2000)141-149.

[150] Ibid.

[151] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 100-102.

المنارة للاستشارات
www.manaraa.com

level of skill and diligence towards the company, as implied in the terms of such a contract.[152]

A director who fails to observe his duty of care and skill will be liable to the company for any loss suffered as a result of such failure.[153] The director's liability will be based either on delict, or if there is a contract between the director and the company, on breach of contract.[154] In *Du Plessis NO v Phelps* (1995 (4) SA 165 (C) at 170) Friedman J explained the position as follows:

> "*Apart from their statutory duties, directors owe fiduciary duties to the company as well as a common law duty to take reasonable care in the management of the company's affairs. Liability in the event of a director failing to take reasonable care in the management of the company affairs is based on the principles of the Lex Aquilia. The basic requisite for liability under the Lex Aquilia is fault, ie dolus or culpa, which results in loss to the plaintiff.*"

As a form of fault, *dolus* usually does not pose any problems when it comes to directors' liability. However, the position with regards to negligence is not as simple. A director will have acted negligently in his duty of care if he failed to do something which a reasonable person would have done under the same instances, or did something that the reasonable person would not have done under the same circumstances.[155] The qualifying phrase "under the same circumstances" indicates the involvement of subjective elements to the objective test. Where the director is an expert, the reasonable person will be placed in the same category namely that of the reasonable expert. Such a director is thus blamed

---

[152] See *Bairstow v Queens Moat Houses plc* [2000] 1 BCLC 549 (QBD). It would appear that the statutory provisions relating to directors' duties in the South African Companies Act 71 of 2008 and the United Kingdom Companies Act 2006 have been codified on this basis.

[153] In most jurisdictions, the law provides for a variety of remedies in the event of a breach by the directors of their duties. The common remedies are injunction or declaration, damages or compensation, restoration of the company's property, rescission of the relevant contract, account of profits or summary dismissal. (Rosenthal A J, Remedies in Disputes Arising Out of Agreements to Buy and Sell Businesses, (1971) *Boston College Law Review,* Vol 12(5) 836-842).

[154] Cilliers *et al*, *Corporate Law*, (2000) 148.

[155] Havenga M, Breach of Directors' Fiduciary Duties: Liability on What Basis? (1996) 8 *South African Mercantile Law Journal* 366.

المنارة للاستشارات
www.manaraa.com

for his carelessness or thoughtlessness in failing to adhere to the standard of care legally required of him.

2.1.3.2 Companies Act 61 of 1973

The above common-law principles governing a director's conduct are amplified by a range of specific duties imposed by statute.[156] Some of these duties are mandatory not to the directors in their own right but to the company. But as the directors are responsible for the performance of the statutory duties imposed on the company, it is they who must make sure that the company does everything that is required of it.[157] The Act does not specifically provide for a director's duty to act with the necessary degree of skill and care but this has been effected through common law. A director may, however, be excused from liability if he or she took reasonably diligent steps to become informed about the matter, has no material financial interest in the matter or had properly disclosed such interest, and made a decision rationally in the belief that it was in the best interests of the company.[158]

Further to the above specific provisions with regards to liability of directors for failure to observe their duties, the Companies Act imputes liability on directors for various offences committed in violation of the provisions of the Act. As an example, sections 423-426 of Companies Act 61 of 1973 provide for personal liability of delinquent directors and others for reckless and fraudulent conduct of company business. The directors may be ordered to restore property and to compensate the company and may be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Court may direct. In terms of these sections,

---

[156] These include the Companies Act (Act 61 of 1973 and Act 71 of 2008) and other legislation like the Public Finance Management Act 1 of 1999 (PFMA), the Municipal Finance Management Act 56 of 2003 and Securities Services Act 36 of 2004.

[157] The majority of the provisions of sections 170-207 of the Companies Act 61 of 1973 provide for liability of any company which fails to comply with any requirement of the sections and every director or officer thereof who knowingly permits or is a party to the failure.

[158] See section 248 of Act 61 of 1973.

المنارة للاستشارات
www.manaraa.com

former directors can be held liable for offences committed during their tenor of office which goes to show the extent of the seriousness the legislators expect directors to carefully and diligently conduct their duties.[159] All these efforts were made to ensure that directors do not abuse their powers, recklessly carry out their duties and that they are held accountable for their actions. This effectively promotes good corporate governance as it encourages upholding of some of the key principles of corporate governance namely transparency, accountability and discipline.

2.1.3.3 Companies Act 71 of 2008

The Companies Act 71 of 2008[160] provides for a director's duty to act with the necessary degree of skill and care expected of a reasonable person.[161] As an enforcement mechanism, where a director does not act reasonably he is liable, in accordance with the principles of the common law relating to breach of fiduciary duty, for any loss, damages or costs sustained by the company as a consequence of any such breach.[162] A director may, however, in terms of the business judgment rule, be excused from liability for breach of the duties of care, skill and diligence and the duty to act in the best interests of the company.[163] In addition, a director is specifically entitled by the business judgment rule to rely on the discharge of functions, and information presented by, persons such as

---

[159] See also *Multi Tube Systems (Pty) Ltd v Ponting and Others* 1984 (3) SA 182 (D) where the Court made it clear that the common-law fiduciary duty of directors owed to the company subsists even after the appointment has ceased.

[160] Section 76.

[161] Section 76(3) of the Companies Act 71 of 2008. To be considered reasonable the director's actions must have been in the interests of the company, the director must have taken diligent steps to understand the subject matter and he must not have a personal financial interest in the subject matter. It is also important that he must have exercised his judgment in a way any reasonable man in similar circumstances would have done.

[162] Section 77 of the Companies Act 71 of 2008.

[163] See section 77(9) of the Companies Act 71 of 2008. The excuse is granted if the director took reasonably diligent steps to become informed about the matter, has no material financial interest in the matter or had properly disclosed such interest, and made a decision rationally in the belief that it was in the best interests of the company. (Havenga M, The Business Judgment Rule – Should We Follow The Australian Example? (2000) 12 *South African Mercantile Law Journal* 25).

المنارة للاستشارات
www.manaraa.com

employees and professional advisers who that director reasonably believes to be reliable and competent.[164]

2.1.3.4 King Report

The new *King Code on Corporate Governance* complements the Companies Act 71 of 2008 and will strongly influence the way that the performance of directors and officers is looked at. Some of the most pertinent provisions relating to directors' duties are also outlined in the *King II* and *King III*, which came into operation in March 2010. Both the *King II* and *III* confirmed the common law position that all directors, both executive and non-executive, have a legal duty to act in good faith, with due care and skill and in the interests of the company.[165] The *King II* provides certain guidelines for directors in performing their duties of care and skill and laid down certain requirements for the acquisition of knowledge, expertise and an understanding of the company affairs. The *Report* explained[166] how these duties should be performed, namely that directors:

"*must, in line with modern trends worldwide, not only exhibit the degree of skill and care as may be reasonable expected from persons of their skill and experience (which is the traditional legal formulation), but must also:*

> • *exercise both the care and skill any reasonable person would be expected to show (in looking after their own affairs as well as having regard to their actual knowledge and experience; and*
>
> • *qualify themselves on a continuous basis with sufficient (at least general) understanding of the company's business and the effects of the economy so as to discharge their duties properly, including where necessary relying on expert advice.*"

---

[164] Davis D *et al*, *Companies and Other Business Structures in South Africa*, (2009) 108-109. Apart from exempting directors from liability, it is argued that the business judgment rule serves to motivate capable persons to undertake the directorship positions and encourages the directors to engage safely in risk taking activities.

[165] Chapter 2 of the *King II* and Chapter 2 of the *King III*.

[166] Chapter 2 of the *King II*.

المنارة للاستشارات
www.manaraa.com

These provisions are similar to the common law and Companies Act provisions discussed above[167] with the difference being that the *King Report* recommendations are not prescriptive in nature.[168]

A further important aspect of the *King II* was the reference to the business judgment rule[169] which originated in the United States of America alongside the duty of care and skill. The motive for developing the rule was basically to protect honest directors from the risks involved in the hindsight appraisal of their ineffective decisions.[170] Taken together, the duty of care and the business rule should ensure that when a decision is taken by a director in accordance with the abovementioned requirements, no liability will arise from that decision however unwise such a decision might have been made.[171] Unlike the *King II Report*, the *King III Report* does not specifically refer to the business judgment rule, but it is assumed that a director would not be held liable for a business decision if such a decision was made on an informed basis, in good faith, without any conflict of interest, and it was rational at the time in all circumstances.[172]

2.1.3.5 Johannesburg Securities Exchange (JSE) Listing Rules

The comments on the *King II* and *III* above with regards to directors' powers and duties equally apply in the case of *JSE Listing Requirements* because the listing rules make it mandatory for companies to comply with and subscribe to certain principles enshrined in

---

[167] Paragraphs 2.1.3.1 - 2.1.3.3.

[168] See paragraph 2.2.2 below where the *King Report* is discussed in more detail.

[169] Ibid.

[170] Essentially the rule protects a director against being held accountable for a business decision if such a decision was made on an informed basis, in good faith, without any conflict of interest, and rational at the time in all circumstances even if it later turns out to have been a wrong decision. See Bainbridge S M, The Business Judgment Rule as Abstention Doctrine, (2004) *Vanderbilt Law Review,* Vol. 57(1) 81-130.

[171] Havenga M, The Business Judgment Rule – Should We Follow The Australian Example? (2000) 25-30.

[172] PricewaterhouseCoopers, *Draft King III at a glance*, available at www.iodsa.co.za/.../Draft%20King%20III%20at%20a%20glance.pdf (visited on 18 October 2009).

المنارة للاستشارات
www.manaraa.com

the *King Report*.[173] Listed entities are required to disclose the extent of their compliance with the *King Report on Corporate Governance* as well as the reason for non-compliance, if any. Naturally, all listed companies are expected to comply with the provisions of the Companies Act because to qualify for listing the business has to be a registered entity in terms of the Companies Act.

2.1.4 Conclusion

The discussion on directors' duties has put the research into perspective by highlighting the general duties of directors which, if properly undertaken, should result in directors practising good corporate governance in that cases of power abuse and excessive remuneration should be minimised. From the discussion, it can be concluded that the rights of directors are relatively modest, while their duties and responsibilities are considerable. Breaches of directors' duties carry sanctions the most severe of which is personal liability, for instance, if they contravene certain provisions of the Companies Act.[174] It is therefore, important that anyone assuming the role of a director should be aware of all the rights and duties of the directors.[175] What is also clear from the discussion is that, although directors are entrusted with the power to manage a company, they are obliged to act both within the powers of the company as well as within their fiduciary duties to the company. Directors are bound by a fiduciary duty and a duty of skill and care to the company in terms of common law, legislation, employment contracts and corporate governance principles. A director's fiduciary obligation thus basically entails that he should exercise his duties in good faith and in the interests of the

[173] Section 8.63(a) of the *JSE Listings Requirements* requires public listed companies, to disclose, in their annual reports and annual financial statements, their measure of compliance with the *King Code*, which is defined in the Listings Requirements as "the Code of Corporate Practices and Conduct representing the principles of good governance as laid out in the *King Report* as amended or replaced from time to time".

[174] Sections 38, 39, 81-86 and 308 of Act 61 of 1973 and section 77 of the Companies Act 71 of 2008 are examples of provisions that make directors liable for contravening the Acts.

[175] Given the common law nature of directors' duties, case law plays a very important role in establishing principles in this aspect of company law. The major concern is that the relevant case law might not be easily accessible to directors. It is however, hoped that with the codification of directors' duties in the Companies Act 71 of 2008, the duties will be easily accessible to the directors who should be constrained to raise a defence of ignorance of what is expected of them. However, it is important to note that partial codification of the duties has its own challenges as it is not always easy to tell when common law is applicable. (Esser I, *Recognition of Various Stakeholder Interests in Company Management*, (2008) 298).

المنارة للاستشارات
www.manaraa.com

company.[176] When a director acts in the company's interests, he should exercise whatever skill he has with the reasonable care expected from a person of his standing.

An important development in the area of directors' duties is the widened definition of "in the interests of the company." Directors are now expected, over and above the profit-maximisation objective, to recognise a wider variety of interests than only those of the shareholders and these interests include, inter alia, environmental interests and those of the investors, employees and consumers.[177] This should have a positive impact on how directors conduct themselves given the possible personal liability they could incur if they failed to observe their duties. Furthermore, directors' duties have been partially codified in the Companies Act 71 of 2008, a development which is expected to improve directors' awareness on their obligations and to make the law accessible.

Having discussed the restraints on directors in the form of duties expected of them, the discussion below seeks to focus on some of the legal and regulatory restraints on directors' powers and remuneration which seek to achieve good corporate governance.

2.2 South African Corporate Governance Legal and Regulatory Mechanisms

2.2.1 Introduction

The corporate governance set-up in South Africa has undergone fundamental changes during the past decade, with the country today being responsive to most corporate governance issues. The segregation of South Africa by the international community during the period of apartheid influenced its businesses and regulators to disregard good corporate management and professional ethics which resulted in poorly governed

[176] In the modern world observing good corporate governance can be interpreted to be acting in the interests of the company as the credibility of the company is enhanced if the directors observe good corporate governance.

[177] Sections 144-146 of the Companies Act 71 of 2008 and Introduction and Background and chapter 8 of the *King III*.

المنارة للاستشارات
www.manaraa.com

companies.[178] South Africa had therefore, to embark on a path of reform after the abolition of apartheid as a result of pressure from international investors, the requirement for external funding and also the need to encourage the highest standard of corporate governance in the country. Although it experienced random setbacks, these reforms have significantly improved the country's standard of corporate governance thus placing South Africa in the top rank of emerging market economies, and in some cases even at par with some of the more developed markets.[179]

Recently, the collapses of some big companies have motivated South Africa to put in place further systems that promote higher standards of ethical conduct, accountability and transparency in companies and by directors.[180] A number of corporate governance misfortunes occurred in the financial sector, resulting in the collapse and absorption of a number of financial institutions.[181] These collapses, among others, highlighted the risk of concentrating power and decision making in the hands of a few individuals which has led to a general consensus around the world that there needs to be balanced powers in companies.[182] In this regard one of the major concerns of corporate governance has been the extent to which executive directors exercise their powers and whether such powers should be restricted.[183]

---

[178] Deutsche Bank Securities Incorporated, *Global Corporate Governance*, *Valuing Corporate Governance in South Africa*, August 19, 2002 available at www.ifc.org/ifcext/corporategovernance.../DB+on+South+Africa.pdf. See also Malherbe S and Segal N, *Corporate Governance in South Africa*, Discussion Document South Africa, OECD Development Centre (2001) available at www.estandardsforum.org/south-africa/.../principles-of-corporate-governance.

[179] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 14-15.

[180] Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, Published MSc Thesis, (UNISA 2008) 1-3.

[181] Smit P J, *Management Principles: A Contemporary Edition for Africa*, (Juta & Co. 2007) 15-18. Examples of financial institutions that collapsed are the Saambou Bank Limited and Regal Treasury Bank.

[182] This is reflected by the number of corporate governance codes the world over which all provide for the need to separate powers between executive and non-executive directors and between the chairman and chief executive officer of a company.

[183] Coyle B, *Corporate Governance*, (2003) 44-51. This aspect of corporate governance is, *inter alia*, about the structure of board of directors, the role of independent non-executive directors and the powers of shareholders under company law.

المنارة للاستشارات
www.manaraa.com

South Africa has responded to the concerns by coming up with a well developed and solid legislative and regulatory corporate governance framework which was established in an effort to restore investor confidence and enhance corporate transparency and accountability.[184] The main sources of corporate governance in South Africa are the *King Reports on Corporate Governance* (which forms the basis of the debate on corporate governance in South Africa), Acts of Parliament, particularly the Companies Act (61 of 1973 and 71 of 2008), common law with rich and extensive case law pertaining to corporate governance and the rigorous *JSE Listings Requirements*.[185] The research dwells much on the *King Reports*, Companies Act, and *JSE Listing Requirements* with brief references to other selected Acts that positively impact on corporate governance. Particular focus will be on those provisions that impact on directors' powers and remuneration and that are aimed at enhancing good corporate governance in South Africa.[186]

2.2.2 King Code on Corporate Governance

2.2.2.1 Introduction

The concept of corporate governance was formally introduced in South Africa in March 1992, with the formation of the King Committee on Corporate Governance whose recommendations made an important contribution to the significant progress South Africa has made towards corporate governance reform since the political transition in the

[184] Estandardsforum Financial Standards Foundation, *Principles of Corporate Governance,* Report on South Africa available at www.estandardsforum.org/servlet (visited on June 13, 2009). The New Partnership for Africa's Development (NEPAD) states that South Africa has adopted the Principles of Corporate Governance designed by the OECD and has made tremendous progress in implementing corporate governance standards and codes (New Partnership for Africa's Development (NEPAD), *African Peer Review Mechanism: Country Review Report of South Africa, September 2007*, (NEPAD 2007) available at http://www.aprm.org.za/docs/SACountryReviewReport5 (visited on June 15, 2009).

[185] Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, (2008) 46.

[186] An assessment on whether the legal and regulatory framework is sufficient to limit directors' powers and regulate their remuneration thereby enhancing good corporate governance will be the subject of the next chapter, chapter 3.

المنارة للاستشارات
www.manaraa.com

mid-1990s.[187] the *King I* served as "a reference point for policy makers in the examination and development of legal and regulatory frameworks for corporate governance."[188] The governance framework proposed by the *King Report* offered the much needed practical guidance to South African private and public institutions in that it was designed specifically to suit local circumstances.[189] The main aim of the *King Report* was to encourage the highest standard of corporate governance in South Africa by recommending standards of conduct for directors and emphasizing the need for responsible corporate conduct.[190]

The adoption of a new Constitution, economic developments locally and internationally as well as consequent overhaul of legislation necessitated the revision of the *King Report*, and the second *King Report (King II*) was published in 2002.[191] The second *King Report* focused more on the qualitative rather than quantitative aspects of good corporate governance in that it extended beyond the existing legal and regulatory framework, and sought to identify key areas of good corporate governance practice which would be voluntarily and effectively applied by companies and directors.[192] The *King II* incorporates a Code of Corporate Practices and Conduct in South Africa which sets out principles which all companies and their boards and directors should observe in conjunction with other statutes, regulations and authoritative directives regulating the conduct of companies, boards and directors.[193]

---

[187] Vallet P, Girard M and Phalane J, *Overview of Recent Corporate Governance Reforms: South Africa*, Fluxmans Inc, available at http://www.globalcorporategovernance.com/n_africa/316_322.htm (visited on 15 July 2009).

[188] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 108.

[189] Mallin C A, *Handbook on International Corporate Governance: Country Analyses*, (Edward Elgar Publishing 2006) 218.

[190] The key challenge for the drafters of the *King I Report* was to seek principles striking an appropriate balance between the freedom to manage, accountability, and the interest of stakeholders, (Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 108).

[191] Mallin C A, *Handbook on International Corporate Governance: Country Analyses*, (2006) 218-219.

[192] Ibid.

[193] Grant Thornton South Africa, *A Brief Overview of King II*, at http://www.gt.co.za/Publications/Effective-directors-guide/kingII.asp (visited on 6 August 2009).

المنارة للاستشارات
www.manaraa.com

The *King II* also focuses on the central role of the board in ensuring good corporate governance and identifies seven fundamental characteristics of good corporate governance namely discipline,[194] transparency,[195] independence,[196] accountability,[197] responsibility,[198] fairness[199] and social responsibility.[200] Given the difficulties of applying the guidelines across the entire South African economy, the *King II* was applicable to all companies listed on the JSE Limited, banks, financial and insurance entities, public sector enterprises falling under the Public Finance Management Act (No. 1 of 1999) and the Local Government: Municipal Finance Management Act (No. 56 of 2003), including any state department acting in terms of the Constitution or legislation.[201] The main reason for the "selective application was to target companies and institutions that fall within a structured and more readily regulated environment in which the corporate governance standards could be more easily identified and measured".[202] All other entities were, however, also supposed to give due consideration to the provisions of the *Report*.

In September 2009, the King Committee on Corporate Governance released the *King III* Code of Governance Principles and the *King III Report* on Governance for South Africa. The issuance of the *King III* was necessitated by the anticipated new Companies Act and changes in international corporate governance trends since the release of the *King II* in

---

[194] *Discipline* refers to a commitment by the company management to adhere to behaviour that is universally accepted.

[195] *Transparency* refers to the ease with which an outsider is able to make meaningful analysis of a company's accounts.

[196] *Independence* focuses on the extent to which mechanisms have been put in place to minimise or avoid potential conflicts of interests.

[197] *Accountability* seeks to ensure that individuals in a company are held accountable for the actions they take.

[198] *Responsibility* pertains to behaviour that allows for corrective action and or for penalising mismanagement.

[199] *Fairness* provides that the systems that exist in a company must be balanced in taking into account all those that have an interest in the company and its future.

[200] *Social responsibility* requires that a well-managed company be aware of social issues and respond thereto.

[201] Langtry S, *Corporate Governance*, (2005) 5.

[202] Mallin C A, *Handbook on International Corporate Governance: Country Analyses*, (2006) 218-219.

المنارة للاستشارات
www.manaraa.com

2002.[203] The *King III* replaced the *King II* as from March 2010 and unlike its predecessors, applies to all entities regardless of their nature, size or form of incorporation or establishment.[204] In a change of approach, the *King III* moves from a "comply or explain" approach to a principles-based "apply or explain" approach.[205] This means that all entities are expected by way of explanation to make a positive statement about how the principles have been applied or have not been applied. A board may therefore conclude that applying a recommended practice is not necessarily in the best interests of the company and apply a different practice provided that it explains the practice adopted and its reasons for doing so. This level of disclosure will allow stakeholders to comment on and challenge the board to improve the level of governance within an organisation. In addition, companies should not necessarily feel an obligation to comply with all aspects of the *King Report*.[206]

The framework recommended by the *King III* is principles-based and acknowledges that there is no "one size fits all" solution.[207] The principles are drafted on the basis that, if they are adhered to, any entity would have practiced good governance. Entities are thus encouraged to tailor the principles of the Code as appropriate to the size, nature and complexity of their organization. This is viewed as a major positive development for

---

[203] The Institute of Directors in Southern Africa and the King Committee on governance, *King III Report on Corporate Governance for South Africa*, 2009.

[204] PricewaterhouseCoopers (PwC), *Corporate Governance in South Africa: A Comparison of the King Report 2002 and The Sarbanes-Oxley Act of 2002*, (PriceWaterhouseCoopers 2002), at http://www.pwcglobal.com/za/eng/inssol/publ/tax/pwc_KingII_vs_SO-2.pdf.(visited on 28 August 2009).

[205] The "apply or explain" approach means that where entities have applied the Code and best practice recommendations in the Report, a positive statement should be made to the stakeholders to this effect and where the entities have not complied with any principle or recommendation they should fully explain the reasons to the stakeholders.

[206] It has been suggested that the term "apply or explain" should be used in preference to "comply or explain", in order to avoid the impression that failure to comply equals non-compliance, that is rule-breaking. Commenting on the effectiveness of the Combined Code, Sir Derek Higgs says "apply or explain" is better than "comply or explain," because "comply" connotes some regulatory compliance or rule where there is none (*The Review on Effectiveness of the Combined Code,* available at www.frc.org.uk/documents/.../Cable%20&%20Wireless.pdf (visited on 15 October 2009).

[207] PricewaterhouseCoopers, *Corporate Governance Series-Draft King III at a glance*, available at http://www.iodsa.co.za/downloads/documents/Draft%20King%20III%20at%20a%20glance.pdf (visited on 10 July 2009).

www.manaraa.com

South African companies as it avoids some of the pitfalls seen in the United States where a "one size fits all" approach was initially adopted.[208]

The *King III* has also broadened the scope of corporate governance in South Africa with its core philosophy revolving around effective leadership, sustainability and corporate citizenship.[209] Leaders are mandated to define strategy, provide direction and establish the ethics and values that will influence and guide practices and behaviour with regard to sustainability performance. The *King III* further highlights, amongst others, the need to improve communications between the board and its stakeholders, matters to do with executive pay, emphasis on non-executive director's effectiveness, integrated reporting, governance within smaller companies and corporate social responsibility.[210]

It is also important to note that the *King III* takes an integrated approach to corporate governance which "recognizes that stakeholders such as the community in which the company operates, its customers, its employees and its suppliers, need to be developed when developing the strategy of the company".[211] The Code thus argues in favour of a balance in corporate governance between allowing directors to run the company in the way they considered best for the stakeholders, while providing stakeholders with some protection against a board of directors that ignores its responsibilities and is not held properly accountable.[212]

---

[208] Deloitte*, Regulatory Review November 2009,* available at www.deloitte.com/.../Regulatory%20Review%20November%202009.pdf (visited on 10 October 2009).

[209] Introduction and background to the *King III*.

[210] CGF Research Institute, *The Case For Good Governance - Past, Present And Future*, available at www.Irca.Co.Za/Docs/14_May_09_The_Case_For_Good_Governance.Pdf (visited on 17 November 2009).

[211] Introduction and Background to the *King III*. See also Hamann R, *South Africa: The Role of History, Government, and Local Context*, (Springer Berlin Heidelberg 2009) 435-439 for a similar line of argument.

[212] Mallette, P, State Anti-corporate Takeover Laws: Issues and Arguments, (1995) *Journal on Managerial Issues,* Vol 7, 142-160.

المنارة للاستشارات
www.manaraa.com

Having discussed the *King Report* in general, what follows is a discussion on the specific recommendations that seek to ensure that directors' powers and duties are carefully and diligently exercised as well as provisions regulating directors' remuneration.

2.2.2.2 Role and Function of the Board

The *King Reports* recommend that the board and its directors should act as the focal point for and custodian of corporate governance and in the best interests of the company.[213] Directors should act in the best interests of the company by, amongst other actions, disclosing conflicts where they exist, dealing in securities only as allowed by internal policies and by adhering to legal standards of conduct.[214] It therefore follows that, to comply with the requirements, directors have to know what is expected of them in so far as performing their duties is concerned. To ensure that directors are adequately guided, the *King II* and *III* recommend that they be properly inducted and trained.[215] In addition, every board should draft a charter setting out its responsibilities which should be disclosed in the annual report and establish the correct balance between conforming with governance constraints and performing in an entrepreneurial manner.[216] The board, through the nominations committee or other board committee should also regularly conduct an evaluation of the board and the individual directors' to assess their effectiveness, independence and whether they have conducted themselves in the interests of all stakeholders.[217] The above recommendations are mainly aimed at ensuring that directors are aware of their duties to the extent that they operate within the confines of their powers as well as in the interests of the company and all stakeholders.

---

[213] Chapter 1 of the *King II* and chapter 1 of the *King III.*

[214] Ibid.

[215] Chapter 2 of the *King II* and chapter 2 of the *King III.*

[216] Ibid.

[217] Chapter 2 of the *King III.*

www.manaraa.com

2.2.2.3. Appointment of New Directors

The *King Report* provides that there should be a formal, rigorous and transparent procedure for the appointment of new directors to the board which should include background and reference checks.[218] It is further provided that appointments to the board should be made on merit and against objective criteria. Unlike the *King II,* the *King III* suggests that the Memorandum of Incorporation of the company should allow the board to remove any director from the board, including executives, without shareholder approval.[219] The board should also make full disclosure regarding individual directors to enable shareholders to make their own assessment of directors. All these provisions are aimed at ensuring that proper and experienced people are appointed as directors who will be able to drive the company towards good corporate governance.

2.2.2.4 Composition of the Board

A key principle of good corporate governance is that there should be a sufficient number of independent,[220] non-executive[221] directors on the board of directors to create a suitable balance of power and prevent the dominance of the board by one individual or by a small number of individuals which may result in abuse of such powers. [222] To ensure that

[218] Chapter 2 of the *King II* and chapter 2 of the *King III.* The main idea behind recommending that there be transparency in the appointment of directors preferably through a nomination committee is to curb potential for corruption in the appointment process, for instance a CEO can nominate directors who may further the board's interest rather than the interests of shareholders and other stakeholders. Boyd indicates three ways in which the nomination of directors who favor the interests of the CEO can be effected namely the CEO can nominate executive directors who are allied to him; the board can also nominate non-executive directors who are not only in favor of the CEO, but who are also financially dependent on the corporation and the CEO may nominate executive and non-executive directors for re-appointment due to the absence of a system that guarantees the rotation of directors. (Boyd, B.K, CEO Duality and Firm Performance: A Contingency Model, (1995) *Strategic Management Journal*, 16, 301-312).

[219] Chapter 2 of the *King III*.

[220] An independent non-executive director is defined in the King *III Report* as a non-executive director who is not a representative of a shareholder, has not been employed by the company/group for the preceding three financial years, is not a professional advisor or significant supplier or customer to the company/group, has no significant contractual relationship with the company/group, is free from any business or other relationship which could influence his independence, does not have a direct or indirect interest in the company and does not receive performance based remuneration.

[221] A non-executive director is an individual not involved in the day to day management of the company and not a full time employee receiving a salary. This definition is similar to that under the *King II*.

[222] Coyle B, *Corporate Governance*, (2003) 63-75.

المنارة للاستشارات
www.manaraa.com

that there is a balance of power within the board and that there is sufficient independence the *King II* and *III Reports* recommend that the board should have a majority of non-executive directors and a sufficient number of non-executive directors should be independent of management.[223] They also recommend that at least one third of the non-executive directors should rotate every year, any independent non-executive director serving more than 9 years should be subjected to a rigorous review of his independence and performance by the board and that the board should include a statement in the integrated report regarding the assessment of the independence of the independent non-executive directors.[224]

The main reason behind engaging non-executive directors is for them to assist companies by checking, with an independent and objective view, whether executive directors duly and diligently exercise the powers vested in them when conducting company business. In addition, independent directors have no contractual relationships with the companies on whose boards they serve and are free from relationships which could interfere with their capacity to act in an independent manner.[225]

The *King Reports* also recommend that the board should be composed of directors who are competent enough to carry out their duties in the interests of the company and to practice good corporate governance.[226] Further to this, the board should make full disclosure regarding individual directors to enable shareholders to make their own assessment of directors. All these recommendations are aimed at ensuring that the composition of directors is such that there is sufficient independence, balance of power and skills to enable effective implementation of good governance principles.

---

[223] Chapter 2 of the *King II* and chapter 2 of the *King III.*

[224] Section 2 chapter 1 of the *King II* and Chapter 1 of the *King III* Code.

[225] Langtry S, *Corporate Governance*, (2005) 8.

[226] Chapter 2 of the *King II* and Chapter 2 of the *King III.* Both the *King II* and the *King III* provide that new and inexperienced directors should be suitably trained through formal induction and mentorship programmes and be updated through regular briefings and continuing professional development programmes so that they are competent enough to carry out their duties.

المنارة للاستشارات
www.manaraa.com

2.2.2.5 Separation of Chief Executive Officer (CEO) and Chairman's Roles

There are two distinct tasks at the top of every company: the running of the board and the executive responsibility for running the company's business.[227] It is argued that the role of the chairman of the company, who is responsible for the former, should be separated from that of the chief executive officer, who is responsible for the latter. What this means is that there should be a clear and unambiguous division of responsibility at the helm of the company to ensure a balance of power and authority.[228] The chairperson of the board plays a central role in ensuring the proper functioning of the board as he acts as an important channel of communication between the board and management of the company. It is the Chairman's duty to ensure that the board is properly briefed on the issues arising at board meetings so that directors are able to ask the right questions and to make informed decision.[229]

The *King II* and *III* Reports state that there should be a clear division of responsibilities at the top of the company, ensuring a balance of power and authority, so that no one individual has 'unfettered powers or authority.'[230] This is aimed at preventing a chief executive officer with a dominating personality imposing his will on the board by acting as chairperson as well.[231] The Codes further state that where the roles of the chairperson and chief executive are combined, there should be either an independent non-executive director serving as deputy chairperson, or a strong independent non-executive director

---

[227] Naidoo R, Corporate *governance: An Essential Guide for South African Companies* (Cape Town: Double Storey 2002) 60-63.

[228] Tumuheki J**,** *Towards Good Corporate Governance: An Analysis of Corporate Governance Reforms in Uganda,* Published MSc Thesis, (University of Cape Town 2008) 32-33.

[229] This was said by Naidoo R while commenting on the recommendations of the *King II* on the role of the chairman and the separation of the role of the chairman and that of the chief executive officer. (Naidoo R, Corporate *governance: An Essential Guide for South African Companies* (2002) 60-63).

[230] Chapter 1 of the *King II* and Chapter 1 of the *King III*.

[231] However, it is pertinent to note that many South African companies still have the same person in the role of both Chairman and CEO and some companies are still to fully implement the recommendations. (Deloitte, *Guide to the JSE Listings Requirements*, available at www.deloitte.com/assets/.../JSE%20Listings%20Requirements.pdf (visited on 22 July 2009)).

المنارة للاستشارات
www.manaraa.com

element on the board.[232] Furthermore, where these roles are combined and where a chairman who is not independent is appointed, this needs to be justified each year in the company's annual report. The *King III* also recommends that the CEO should not become the chairman until 3 years have lapsed. This was not a requirement in the *King II*.

2.2.2.6 Board Committees

Under the *King III Report*, a number of board committees are provided for,[233] with supervisory functions over particular areas, namely the audit committee;[234] the risk committee;[235] the nomination committee and the remuneration committee.[236] It is important to note that, although the boards of directors are encouraged to delegate responsibilities to committees the board of directors still remains responsible for the company thus cannot wholly abdicate its responsibilities.[237]

Both the *King II* and *King III Reports* further recommend that audit, nominating and remuneration committees should be composed of independent non-executive

[232] Chapter 1 of the *King II* and Chapter 1 of the *King III*.

[233] The *King II* required that, at a minimum, companies have an audit and remuneration committee.

[234] Chapter 3 of the *King III*. According to the *King III* an audit committee is appointed "to assist the board in discharging its duties relating to the safeguarding of assets, the operation of adequate systems, control processes and the preparation of accurate financial reporting and statements in compliance with all applicable legal requirements and accounting standards".

[235] Chapter 4 of the *King III*. The risk committee is primarily tasked with (i) reviewing the risk management progress and maturity of the company; (ii) the effectiveness of risk management activities; (iii) the key risks facing the company; and (iv) the responses to address these key risks.

[236] Chapter 2 of the *King III*. The function of the remuneration committee is to assist the board in setting and administering remuneration policies for all levels in the company, but should be especially concerned with the remuneration of senior executives.

[237] Chapter 2 of the *King III*. T Wixley and G Everingham argue that the main reason for board committees is that "the board of directors of a typical listed company meets together for less than 24 hours a year, a surprisingly short time to accomplish all that is expected of it." Given that the time available to the board to accomplish all its tasks in a single meeting is not sufficient, some issues need to be dealt with in a focused way at committee level, and then later presented to the board as a whole. (Wixley T. and Everingham G, *Corporate Governance,* 2nd Edition (Siber Ink CC, South Africa 2005) 58).

المنارة للاستشارات
www.manaraa.com

directors.[238] The *King Report* recommends that board committees should have clear mandates and areas of authority including written terms of reference, which should specify their composition, role and responsibilities, objectives, powers and authority, term of existence, the frequency of their meetings, and the manner in which reports back to the full board are to be dealt with.[239] These committees can therefore be understood as serving a *de facto* supervisory role in relation to any company actions taken with regard to that particular function. In particular, the existence of a sound audit function is regarded as crucial to good corporate governance as it provides an important channel of communication between the board, management, and the internal and external audit functions of the company.

2.2.2.7 Compliance with Laws, Rules, Codes and Standards

The board and each individual director should ensure that the company complies with applicable laws and adheres to nonbinding rules, codes and standards.[240] Directors are thus expected to ensure that whenever they exercise their powers they comply with all applicable laws and regulations. Directors have an obligation to acquaint themselves with the general content of applicable laws, rules, codes and standards in order to efficiently discharge their legal duties and to exercise their powers within the confines of the relevant laws and regulations.[241] It is, however, important that there is substantive compliance with the rule and not just with the form of corporate governance so "Box ticking"[242] should be avoided at all costs.

---

[238] Chapter 2 of the *King II* and Chapter 2 of the *King III*. See also Colley et al, *Corporate Governance*, (2003) 3-7.

[239] Chapter 2 of the *King II* and Chapter 2 of the *King III*.

[240] Chapter 6 of the *King III*. The compliance with laws, rules, codes and standards has always been an explicit statutory requirement but the *King III* now provides recommended principles and practices that can be adopted to ensure that compliance is achieved.

[241] Chapter 6 of the *King III*. To assist directors in achieving this, both the *King II* and *King III* provide that the induction and ongoing training programmes of directors should incorporate an overview of and any changes to applicable laws, rules, codes and standards.

[242] Box-ticking refers to the situation where corporate governance boxes are ticked, indicating that there was compliance with a specific aspect.

المنارة للاستشارات
www.manaraa.com

To ensure that directors comply with the relevant laws and regulations, the *King Reports* further recommend that companies should establish an internal audit function[243] which should be objective and independent of management.[244] The *King II* and *III* further provide for the engagement of external auditors[245] who are tasked with a statutory duty to report their independent opinion on the accuracy and completeness of company's financial statements to the shareholders and on the compliance by the directors with the relevant laws and regulations. The internal audit, external audit and board audit committees are essential parts of the checks and balances required in ensuring that directors operate within their mandates, comply with all laws and regulations, report accurately in financial statements and uphold the principles of corporate governance.

2.2.2.8 Shareholder Participation

As another checking mechanism, the *King Reports* recommend that shareholders be encouraged and allowed to actively participate in the affairs of the company so that they are able to detect any abuse of authority early enough to prevent it and also to give appropriate guidance to directors.[246] To encourage shareholder activism, the *King Report* recommends; educating shareholders in corporate governance, introduction of class actions and a contingency-fee system to encourage legal action, review of quorum requirements to encourage participation at general meetings, establishment of shareholder watch-dog organizations to look after the interests of minority shareholders, and the role of institutional investors in achieving successful corporate governance.[247]

---

[243] Chapter 7 of the *King II* and chapter 7 of the *King III*.

[244] Chapter 7 of the *King III*. The audit function should "evaluate the company's governance processes, perform an objective assessment of the effectiveness of risk management and the internal control framework, systematically analyse and evaluating business processes and associated controls; and provide a source of information as appropriate, regarding instances of fraud, corruption, unethical behaviour and irregularities."

[245] Chapter 3 of the *King II* and chapter 3 of the *King III*.

[246] Chapter 8 of the *King II* and chapter 8 of the *King III*.

[247] Introduction and Background to *King III Report*. See also Institute of Directors in Southern Africa, *Executive Summary of the King Report 2002*, (IOD 2002) available at www.iodsa.co.za (visited on 25 June 2009).

المنارة للاستشارات
www.manaraa.com

The main emphasis is on enhancing the responsibility and accountability of boards of directors.

Following the realization of the importance of shareholders in promoting good corporate governance, a number of initiatives have been proposed and others implemented, for instance, shareholders now have to vote and agree on each board's remuneration policy.[248] They need to vote in directors individually, rather than in a bloc,[249] and they have the responsibility to appoint an audit committee.[250] They are entitled to receive satisfactory explanations as to why the company has decided to grant shares options to non- executive directors before they approve the granting of the share options.[251] Therefore, if shareholders effectively exercise their rights they become an essential checking mechanism to curb abuse of power and excessive payment of salaries by directors.

2.2.2.9 Conclusion

The discussion above shows that South Africa, through the *King Report* has tried to limit the directors' powers by recommending a rigorous and transparent procedure for the appointment of directors, a properly balanced board to prevent dominance by one individual, separation of the CEO and chairman's roles and encouraging shareholder participation, among others. Whilst it is acknowledged that these provisions have significantly contributed to the limiting of directors' powers what remains to be examined is whether these recommendations are sufficient or not in promoting good

[248] Chapter 2 of the *King III*.

[249] Chapter 2 of the *King III*. The Code provides that the board should make full disclosure regarding individual directors to enable shareholders to make their own assessment of directors.

[250] Chapter 2 of the *King III*. The Companies Act 71 of 2008 has made the Audit Committee of public companies and state-owned companies a statutory committee. With regard to its statutory duties, the Audit Committee is accountable to the shareholders and has sole authority to make decisions on these statutory duties specifically defined in the Act i.e. where there is a conflict between the Board and the Audit Committee on the Audit Committee's statutory duties, the Audit Committee's decision will prevail.

[251] Chapter 2 of the *King II* and Chapter 2 of the *King III*.

www.manaraa.com

corporate governance. The sufficiency of the *King Report*'s recommendations is the subject matter of chapter 3.

2.2.3 The Companies Act

2.2.3.1 Introduction

The Companies Act 61 of 1973 and common law were South Africa's corporate governance references before the *King I Report*.[252] The Act has been in existence since 1973 and imposes a number of statutory duties on directors which if properly observed will result in good corporate management. It governs how companies should be administered and provides for regulation of powers, duties and remuneration of directors.[253] However, the Act does not specifically provide for corporate governance but it imputes liability on directors if it is found that directors conducted the business of the company fraudulently or recklessly.[254] It can be argued, for example, that ignoring good corporate governance principles may amount to fraud and/or recklessness.[255] This

[252] Naidoo R*, Essentials of Corporate Governance for South African Companies*, (2002) 10.

[253] Sections 170 – 251 of Act 61 of 1973. Sections 170 -207 provide for administration of companies which include general administration, meetings of companies and voting at meetings. Sections 208 -251 provide for appointment of directors, their duties including the duty to declare interests, restrictions of their powers and prohibitions to make certain payments to themselves.

[254] Section 424 of Act 61 of 1973 provides for personally responsibility, without any limitation of liability of directors for fraudulent conduct of business when it appears that any business of the company was carried on recklessly, with intent to defraud creditors of the company or for any fraudulent purpose.

[255] Vallet *et al*, *Overview of Recent Corporate Governance Reforms: South Africa*, 8. See also *Minister of Water Affairs and Forestry V Stilfontein Gold Mining Co Ltd and Others* 2006 (5) SA 333 (W) where the directors were fined for violating their environmental obligations. In this case the Court found that the directors of a company, who all resigned simultaneously, in order to avoid taking certain action, acted in bad faith to the company and were liable for the consequences of not discharging their duties. It appeared from the evidence that all directors had resigned from their positions on legal advice to the effect that if they continued in office the mine's non-compliance with the court order might render them party to reckless trading. In passing judgment the court considered that the code of conduct of the second *King Report* was almost uniformly endorsed by the corporate community in South Africa and that the conduct of the respondent directors was part of their responsibilities in terms of the *King code of conduct*, which they were obliged to implement by virtue of the fact that the respondent was a listed company and consequently had to adhere to the *Listing Requirements* of the JSE Securities Exchange. The court held all the respondents guilty of contempt of court. It is therefore, important to note that, although the *King Report* is still self-regulatory, the court referred extensively to the second *King Report* to determine if the directors had breached their duties.

www.manaraa.com

provision is therefore an enforcement mechanism that can be used to ensure good corporate governance practices.

Due to a new political dispensation, greater international participation and foreign investment, corporate governance initiatives, and the changed constitutional framework a comprehensive review of South Africa's company legislation became both unavoidable and necessary.[256] It was also important that South African company law be harmonised with current national and international laws and economic developments and trends.[257] This brought about the signing of a new Companies Act 71 of 2008 into law in 2009. In terms of the government policy statement issued before the promulgation of the new Act, the revised company law is expected to promote the competitiveness and development of the South African economy. This will be achieved by, among other ways, promoting innovation and investment in South African markets and companies by providing a predictable and effective regulatory environment that allows for growth, flexibility, transparency, good governance and ensures compatibility and harmonisation with best practice internationally.[258]

Following is a discussion of some of the Companies Act provisions which have a bearing on directors' duties and powers in so far as the enhancement of corporate governance is concerned and which have the effect of curtailing directors' powers and deterring them from breaching their duties.

[256] Institute of Chartered Secretaries and Administrators of South Africa, *Codification,* Presentation to the Department of Trade and Industry on the Draft Companies Bill, March 2007 available at http://www.icsa.co.za/assets/presentations/companiesbill/final.pdf. (visited on 15 September 2009).

[257] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 96.

[258] *South African Company Law for the 21st Century Guidelines for Corporate Law Reform*, General Notice 1183 of 2004, 8-9.

المنارة للاستشارات
www.manaraa.com

2.2.3.2 Codification of Directors' Duties

As indicated above, the Companies Act 71 of 2008 proposes to enhance corporate accountability and transparency by partially codifying[259] directors' duties and specifically setting a standard of directors' conduct so that the directors are aware of their duties and responsibilities. The directors will thus find it difficult to allege that they were unaware of their obligations if challenged for violating their fiduciary duties and the duty of skill and care expected of them.

Although it has been questioned whether it is necessary to codify directors' duties as a way of encouraging a higher standard of conduct by directors, it is considered by some as a very good starting point or even a necessity as they argue that the current standards are inadequate, outdated and are scattered in a mass of decided cases which may not be easily accessible to both directors or stakeholders of the company.[260] Michele Havenga[261] argues that partial regulation is the most appropriate for South Africa as it serves the purpose of making the law understandable and easily accessible,[262] whilst retaining some flexibility. She further argues that codification of directors' duties will not only make the law accessible and go some way to ensure that directors are clear about their obligations, but it will explain to foreign and local investors the rules that govern the behavior of directors and the associated liabilities or remedies in case of violation of those rules.[263] Other commentators also argue that codification will compel

---

[259] Partial codification, unlike complete codification, involves adopting the general principles of law but allows some room for the development of the common law.

[260] Mackenzie A. L, A Company Directors' Obligations of Care and Skill, (1982) *Journal of Business Law* 460.

[261] Havenga M, *Regulating Conflicts of Interest and South African Company Law Reform,* UNISA, available at http://www.law.usyd.edu.au/parsons/CLTA/HavengaPaper.pdf, at 7, (visited on 22 June 2009).

[262] Directors need to know what their duties are, and directors must be aware of what is expected of them, because the standards of director's conduct can influence the profitability of a company, determine the extent of foreign and domestic investments and ultimately determine the success of a company. (Kiggundu J & Havenga M, The regulation of directors' self-serving conduct: perspectives from Botswana and South Africa, (2004) *Comparative and International Law Journal of Southern Africa,* Vol. 37(3) 312-326).

[263] Havenga M, *Regulating Directors' Duties and South African Company Law Reform*, UNISA 2005 available at www.sabinet.co.za/abstracts/obiter/obiter_v26_n3_a13.xml.

المنارة للاستشارات
www.manaraa.com

directors to act in accordance with professional standards of care and to make proper and sound business decisions.[264]

Those against codification of directors' duties, on the other hand, argue that the common law adequately defines and deals with directors' duties and liabilities such that codification of those duties would be unnecessary and inadequate to address the dynamics of directors' duties.[265] Their line of argument is that it is practically impossible to impose uniform standards on directors due to the differences in the type of decisions directors have to make and also differences in the nature of business conducted by the companies. They also believe codification creates unnecessary rigidity and conciseness which may cause directors, for instance, to consider the omission of important requirements from legislation as making the omitted requirements of less value and to disregard some duties and obligations which may be contained in other legislation and regulations.[266] This confirms the view that was expressed in respect of the United Kingdom company law reform that it would be almost impossible to comprehensively codify directors' fiduciary duties and their obligations of care and skill as there are simply too many matters to be taken care of.[267]

They further contend that directors might not be prepared to take the necessary risks and to fully engage their entrepreneurial abilities for their companies' economic growth but might just concentrate on observing formalities.[268] However, it is important to note that,

---

[264] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 113-114.

[265] Ibid.

[266] Esser I, *Recognition of Various Stakeholder Interests in Company Management*, (2008) 291-292.

[267] See Berg A, The Company Law Review: Legislating Directors' Duties, (2000) *Journal of Business Law* 472, where Berg points out several difficulties with the codification of directors' duties and Birds J, "Reform of Directors' Duties", in De Lacy L (ed) *The Reform of United Kingdom Company Law* (Cavendish Publishing 2002) which mentions several of the issues that have to be dealt with.

[268] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 113-114.

المنارة للاستشارات
www.manaraa.com

although directors' duties have been codified, the continued applicability of common law[269] will assist in ensuring that the duties remain flexible and adaptable to changes.

Despite the concerns above, it is important to note that the Companies Act 71 of 2008 provides for various directors' duties which encourage integrity, transparency and accountability (some key elements of corporate governance). For example, directors have a duty to ensure that all company profits are detailed and accounted for,[270] thereby ensuring accountability. Directors have a duty to exercise an independent and unfettered discretion,[271] which encourages a culture of integrity. Moreover, directors also have a duty to disclose any interests they may have in a contract with a company,[272] thereby encouraging transparency.

2.2.3.3 Board Committees

Pursuant to section 72 of the Companies Act 71 of 2008, a company board may appoint committees comprised of directors, and "delegate to any committee any of the authority of the board". Like in the *King Code* board committees are, among other functions, expected to play a supervisory role on executive directors and management on behalf of the main board.

As a result of the recommendations of the King Committee,[273] the Companies Act 71 of 2008 contains a provision for a statutory requirement of an audit committee.[274] Section 94 of the Companies Act provides that the board of a company may appoint an audit committee comprising at least three members and delegate any of the authority of the

---

[269] See section 76 of the Companies Act 71 of 2008.

[270] Section 30 of the Companies Act 71 of 2008.

[271] Ibid.

[272] Section 75 of the Companies Act 71 of 2008.

[273] Chapter 3 of the *King III*.

[274] Section 94 of the Companies Act 71 of 2008.

المنارة للاستشارات
www.manaraa.com

board subject to any limitation in the company's Memorandum of Incorporation.[275] The committee members must be directors of the company but not involved in the day-today management of the company or related to any person involved in management of the company.[276] The section further requires members of the audit committee to act independently in the performance of the committee's functions.

The setting up of an audit committees is an important checking mechanism on directors' powers and remuneration as the committee can, independent of executive directors, receive and deal appropriately with any concerns or complaints, whether from within or outside the company, or on its own initiative.[277] It has, however been argued that the danger of incorporating corporate governance requirements into legislation will have the effect of making the omitted requirements appear to be of less value.[278] According to this argument, the inclusion of the audit committee into the Companies Act will make other committees appear less important.

2.2.3.4 Shareholder Participation

While the Companies Act 71 of 2008 only changes the general duties of directors to a smaller degree, it most certainly increases the burden of the office of director by enhancing the rights of shareholders and other stakeholders. The Companies Act 71 of 2008 promotes and encourages transparency and high standards of corporate governance through greater director accountability and the appropriate participation of all stakeholders.[279] Shareholder participation at general meetings of the company is

[275] See also section 72 of the Companies Act 71 of 2008.

[276] Ibid.

[277] Section 94(7)(g) of the Companies Act 71 of 2008.

[278] Institute of Chartered Secretaries and Administrators of South Africa, *Presentation to the Department of Trade and Industry on the Draft Companies Bill*, March 2007 at 1 available at http://www.icsa.co.za/assets/presentations/companiesbill/final.pdf. (Visited on 12 August 2009).

[279] Key provisions in the new Act will raise directors' accountability to shareholders (sections 75-77) and increase the likelihood of shareholders participating in legal action, particularly if the company and its officers caused shareholders to suffer significant financial loss (sections 161-165).

المنارة للاستشارات
www.manaraa.com

modernised and clearly set out in the Act.[280] The Act also allows participation of shareholders other than at a meeting,[281] which is one of the areas where the 1973 Companies Act has always been inflexible.

The Act gives more extensive rights to shareholders in respect of meetings and governance of companies. In terms of the Companies Act 71 of 2008 shareholders have a right to access company records,[282] to receive a notice of the publication of any annual financial statements of the company required by the Act[283] and to participate in, and speak and vote at, a shareholders meeting in his personal capacity or represented by a proxy.[284] Shareholders are also likely to invoke the Act's new procedures for seeking the removal of a director from the board of a company[285] or applying to court for an order declaring a director to be delinquent or under probation.[286] These rights will not only enhance the control of shareholders over management but will also place management under the spotlight in the execution of their duties.

---

[280] Sections 58-65 of the Companies Act 71 of 2008.

[281] Section 60 of the Companies Act 71 of 2008.

[282] Section 26 of the Companies Act 71 of 2008. Furthermore, in South Africa, section 32(1) (b) of the Constitution provides that everyone has the right of access to information held by another person when such information is required for the exercise or protection of any rights. The Promotion of Access to Information Act 2 of 2000 (PAIA) was enacted to give effect to this right (Section 50 of PAIA).

[283] Section 31 of the Companies Act 71 of 2008.

[284] Sections 58-65 of the Companies Act 71 of 2008.

[285] Section 71 of the Companies Act 71 of 2008 empowers shareholders to remove a director by an ordinary resolution adopted at a shareholders meeting.

[286] Sections 162-165 of the Companies Act 71 of 2008. Currently, a shareholder's relationship with the company means that they can't, generally speaking, bring an action against officers directly. They have to request the company to bring a law suit against an officer who committed a wrongful act. However, directors and company officers are unlikely to bring an action against their colleagues, and therefore shareholders have limited recourse to recover damages from wrongful acts committed by company officers. Under the new Act, shareholders will have direct recourse against directors and officers in a personal capacity as long as they can prove they have suffered damages.

المنارة للاستشارات
www.manaraa.com

2.2.3.5 Conclusion

Like the *King Report*, the Companies Act provides for limitation of directors' powers through, among others, codification of directors' duties, providing for board committees that supervise executive directors, encouraging shareholder participation and through stiff penalties for abuse of directors' powers. The adequacy of the Companies Act in limiting directors' powers and promoting good corporate governance is discussed in chapter 3 below.

2.2.4 Other Acts

2.2.4.1 Introduction

The KPMG 2004 Survey of Integrated Sustainability Reporting in South Africa notes that from 1994 to 2004 approximately 60 Acts were passed or substantially revised which had a direct impact on corporate governance. These include (as amended) the Labour Relations Act 66 of 1995, the Basic Conditions of Employment Act 75 of 1997, the Employment Equity Act 55 of 1998, the National Environmental Management Act 107 of 1998, Public Finance Management Act 1 of 1999, the Promotion of Access to Information Act 54 of 2002, the Securities Services Act 36 of 2004 and the Constitution of the Republic of South Africa 108 of 1996.[287]

There has also been a comprehensive update of the provisions and regulations governing the Banks Act 94 of 1990, which substantially enforces higher levels of corporate governance[288] and risk reporting in banking institutions.[289] As a result, the country's

---

[287] Sarra, J. P, *Strengthening Domestic Corporate Activity in Global Capital Markets: A Canadian Perspective on South Africa's Corporate Governance*, The George Washington University Law School Public Law and Legal Theory Working Paper No 118, Institute for International Corporate Governance and Accountability, (2004), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=628702. (Visited on 29 August 2009).

[288] This introduced a number of mandatory provisions of a governance nature, and codified the duty of care expected of a bank director and certain categories of executives in relation to shareholders and depositors.

[289] King Committee on Corporate Governance, *Executive Summary of the King Report 2002*, available at www.ecgi.org/codes/documents/executive_summary.pdf (visited on 15 November 2009).

المنارة للاستشارات
www.manaraa.com

financial services sector is well developed and its financial system is complicated and compares well with those in the developed world.[290] In addition, a series of statutory interventions and regulations have also been introduced to fight money laundering and support stricter anti-corruption measures.[291] These are not only in line with the priority accorded to good governance, but advertise South Africa's intention to observe international conventions and standards so as to add credibility to the country's international standing. Judging from the number of statutes that provide for good corporate governance it would appear that South African politicians and policy makers are determined to minimize the risk of future incidents of serious corporate failures and will thus continue to formally incorporate key provisions of the *King Reports* in the wide ranging body of laws and regulations.

Following are brief discussions on some of the Acts listed above that have an impact on corporate governance.

2.2.4.2 Securities Services Act 36 of 2004

In an effort to fight insider trading and enhance corporate governance in South Africa's capital markets, the South African government passed the Securities Services Act in 2004 and established the Insider Trading Directorate within the Financial Services Board (which supervises the non-banking financial services industry) to monitor and enforce the law.[292] The Security Services Act makes it a criminal offence for anyone to make use of "inside information"[293] to buy or sell any securities or financial instruments in a

---

[290] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 23-25.

[291] Mallin C A, *Handbook on International Corporate Governance: Country Analyses*, (2006) 218-221.

[292] The Insider Trading Directorate established by section 12 of the Insider Trading Act continues to exist, despite the repeal of that Act by section 117 of the Securities Services Act and is now called Directorate of Market Abuse.

[293] In terms of the Securities Services Act 36 of 2004 "inside information" means "specific or precise information which has not been made public and which-
(a) is obtained or learned as an insider; and
(b) if it were made public would be likely to have a material effect on the price or value of any securities or financial instrument."

المنارة للاستشارات
www.manaraa.com

company in a regulated stock market.[294] The Act plays an important role in restraining directors from abusing the privilege they have to obtain inside information about their companies before the outsiders. In practice, however, there have been relatively few successful criminal prosecutions of individuals for insider dealing, because the guilty of an alleged "insider dealer" has been difficult to prove in specific cases. [295]

For the first time in South African legislation the Act extended beyond criminal sanction to embrace civil remedies.[296] Under the civil provision, a person will be compelled to surrender his gains and may also be penalized up to three times the amount of any profit so earned.[297] A person prosecuted under the criminal provision may be fined up to R50, 000,000 and imprisoned up to ten years.[298] The introduction of a civil offence is considered significant because, previously, prosecutors were only able to proceed under the criminal provision of the Companies Act and due to the fact that criminal offences require a higher standard of proof, few charges were filed in courts with virtually no successful prosecution under the criminal provision.[299] It is important to note that since the promulgation of the Insider Trading Act in 1998, the Insider Trading Directorate has, despite limited prosecutorial resources, experienced some success in that it has managed to settle a number of civil suits in which fines were imposed and to initiate a few criminal cases.[300]

---

[294] Section 73 of the Securities Services Act 36 of 2004.

[295] Loubser R, *Insider Trading and Other Market Abuses (Including the Effective Management of Price Sensitive Information)* available at http://www.jse.co.za/Libraries/JSE_-_(visited 10 October 2009).

[296] Section 77 of the Securities Services Act provides for civil liability of inside traders. See also Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 15.

[297] See section 77(1) of the Securities Services Act.

[298] See section 115 of the Securities Services Act.

[299] Loubser R, *Insider Trading and Other Market Abuses (Including the Effective Management of Price Sensitive Information*, 10-18.

[300] In the first six months of operation the Insider Trading Directorate achieved six settlements and in the following three months it proceeded with two further civil suits and one criminal prosecution. (Malherbe S. and Segal N, *Corporate Governance in South Africa,* 2007). However, even with the new insider trading law in place, there is a persistent worry among investors that unlawful insider trading still occurs. While the Insider Trading Directorate has made strides to prosecute insider trading offenses, there are still instances, such as in the case of Saambou, where the share prices of certain companies fall a day or two prior to the announcement of a profit warning.

المنارة للاستشارات
www.manaraa.com

2.2.4.3 Public Finance Management Act 1 of 1999

Many principles in the *King Report* have been adapted for the public sector via the Public Finance and Management Act (PFMA) which, in terms of section 3, is applicable to constitutional institutions such as the Electoral Commission (IEC) and all government departments and public entities at national and provincial levels. The Public Finance Management Act introduced much more comprehensive standards for reporting and accountability by adopting an approach to financial management in public sector institutions that requires performance in service delivery, and economic and efficient deployment of state assets and resources.[301] In the public sector, the PFMA, which incorporates certain aspects of the *King II*, plays an important role in regulating good corporate governance practices.[302] The PFMA aims to secure transparency, accountability, and sound management of the revenue, expenditure, assets and liabilities of the institutions to which the Act applies.[303] An official of a department or trading entity or constitutional institution to whom a power or duty is imposed in terms of the Act commits an act of financial misconduct if the officer willfully or negligently fails to exercise such power or perform such duty.[304] To further enhance compliance, section 86 of the Act also provides for criminal liability of accounting officers and authorities who willfully or grossly negligently fail to comply with certain provisions of the Act.

To complement the Act, a government policy protocol that laid down comprehensive guidelines for good corporate governance in public sector institutions was produced. The protocol set standards of conduct and good governance the government expected its public institutions and officials to comply with.[305] Further to the Public Finance

---

[301] Langtry S, *Corporate Governance,* (2005) 5.

[302] PricewaterhouseCoopers (PwC), *Corporate Governance in South Africa: A Comparison of the King Report 2002 and The Sarbanes-Oxley Act of 2002*, (2002) 6-7.

[303] See preamble and section 2 of the Public Finance and Management Act 1 of 1999.

[304] Sections 81-85 of the Public Finance and Management Act 1 of 1999.

[305] Mallin C A, *Handbook on International Corporate Governance: Country Analyses*, (2006) 218-219.

المنارة للاستشارات
www.manaraa.com

Management Act, the South African government also introduced the Municipal Finance Management Act 56 of 2003 which imposes extensive governance obligations on officials and executives associated with municipal financial administration.[306] This is a clear signal from policy-makers that corporate governance has been identified as a matter of national significance and not just for the private institutions.

2.2.4.4 Broad-Based Black Economic Empowerment Act 53 of 2003

Black Economic Empowerment[307] has been a major policy thrust of the democratic government in South Africa since 1994 in attempting to redress the effects of apartheid and to encourage effective participation in the economy by previously disadvantaged people. A number of statutory measures[308] and various self-regulatory sectoral accords, such as those reached in the mining and finance sectors have been designed to address historical socio-economic imbalances. It has, however, been by and large accepted that so far the measures have not been as successful in ensuring broad-based participation of black people in the economy as desired.[309]

The Broad-Based Black Economic Empowerment Act was thus passed to set up a legal framework for the promotion of black economic empowerment so that black people have sufficient influence over strategic direction and core management of businesses.[310] The Act seeks to "promote the achievement of the constitutional right to equality, increase broad-based and effective participation of black people in the economy and promote a higher growth rate, increased employment and more equitable income distribution; and

---

[306] See section 2 of the Act for its objectives and section 3 for details of the institutions to which Act applies.

[307] See section 1 of Broad-Based Black Economic Empowerment Act 53 of 2003 for definition of "broad-based black economic empowerment".

[308] Examples are the Employment Equity Act 55 of 1998; Promotion of Equality and Prevention of Unfair Discrimination Act 4 of 2000 and the Land and Agricultural Development Bank Act 15 of 2002.

[309] Havenga M K, *Regulating Directors' Duties & South African Company Law Reform*, (2005) 26 Obiter 609, 618.

[310] Southall R, The ANC and Black Capitalism in South Africa, (2004) *Review of African Political Economy* 100, 313-328.

المنارة للاستشارات
www.manaraa.com

establish a national policy on broad-based black economic empowerment so as to promote the economic unity of the nation, protect the common market, and promote equal opportunity and equal access to government services."[311] It provides for, *inter alia,* issuance of Codes of good practice[312] and transformation charters.[313] The Codes of good practice provide detailed regulations and guidelines on black economic empowerment as well as a framework for measuring progress made on the implementation of the black economic empowerment measures.[314] The Broad-Based Black Economic Empowerment Act is one of the statutes that oblige companies and their directors to "consider the broader South African community within its political and socio-economic context".[315]

Some commentators argue that, in pure governance terms, some of the steps taken to bring about black economic empowerment might present challenges for corporate governance in that "the process of building a capitalist class on the basis of artificial financing structures can, all too readily, lead to business ventures with shareholding structures that transgress the principles of good governance."[316] The matter is further complicated by the fact that South Africa already does not have sufficient skilled and competent directors, a situation which might be worsened if the pool of directors is limited to only black entrepreneurs whose supply may not match the demand. There is therefore, need for careful management of priorities so as to balance best business practice and this type of affirmative action which has many strategic merits. This can only be achievable if cautious decisions and strategies are made by policy-makers and everybody else to ensure that the commendable efforts made towards the empowering of

---

[311] See Preamble to Act 53 of 2003 and section 2 of the same Act for the objectives of the Act.

[312] Section 9 of Act 53 of 2003.

[313] Section 12 of Act 53 of 2003. An example is the Broad-Based Socio-Economic Empowerment Charter for the South African Mining Industry, which provides that companies must report on an annual basis their progress toward achieving their commitments to the objectives set out in the Charter.

[314] Esser I & Dekker A, The Dynamics of Corporate Governance in South Africa: Broad Based Black Economic Empowerment and the Enhancement of Good Corporate Governance Principles, (2008) 164.

[315] Ibid. Failure by a company and its directors to comply with the requirements of the Act may result in unfavorable ratings which may affect the company's capacity to do business in South Africa.

[316] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 32-35.

المنارة للاستشارات
www.manaraa.com

the previously disadvantaged people do not frustrate the drive for good corporate governance.[317]

2.2.4.5 Conclusion

This general discussion on other Acts that provide for directors' duties highlights the point that directors are expected to observe a number of other statutory duties besides those provided for in the Companies Act. As discussed in paragraph 2.2.2.7, good corporate governance is also about complying with the relevant laws, rules, codes and standards which means directors are expected to comply with the provisions of these other Acts. The other Acts, therefore, also assist in limiting the way directors exercise their powers for example, the Insider Trading Act prohibits directors from misusing share information obtained during the course of their duties. However, the effectiveness of these Acts in restricting directors' powers have their own limitations as shown in chapter 3 below.

2.2.5 The JSE Listings Requirements

2.2.5.1 Introduction

The development of corporate governance in South Africa has manifested itself in a number of interesting ways. Worth noting among these has been the movement of the primary listings offshore by some of South Africa's major companies to international financial centres such as London and New York.[318] The main reasons given for moving are not really a result of any discontentment at prevailing governance structures in South

[317] Ibid.

[318] Carmody P, Between Globalisation and (Post) Apartheid: the Political Economy of Restructuring in South Africa, (2002) *Journal of Southern African Studies*, Vol 28(2) 1465-1493. Some of South Africa's largest companies that have moved their primary listings abroad, particularly to the London Stock Exchange are Anglo American, SAB, Old Mutual, SA Breweries and Billiton. Another clear illustration is provided by the withdrawal by Telkom (a former government parastatal) of its majority-owned mobile telephone operator, Vodacom, from the Nigerian market because of doubts relating to the integrity of certain local business dealings.

المنارة للاستشارات
www.manaraa.com

Africa, but rather the desire to lure investors in an arguably, more stable currency environment and to obtain cheaper funding.[319] A major effect, however, has been a growing appreciation in these companies of the high standards of governance required to operate with credibility in international markets, the desire of these companies to associate themselves with markets with stronger corporate governance reputations and the consequent introduction of those higher standards into their operations in South Africa.[320] The other favourable effect is that foreign listing of shares by South African companies has forced the JSE and the South African authorities to upgrade their corporate governance standards.[321] To confirm the extent of movement internationally, it is reported that in 2002 there were more than 65 JSE-listed companies that maintained primary or secondary listings outside of South Africa.[322]

The *JSE Listings Requirements* have been amended to further align them with international best practice, thereby aiming to enhance the status of JSE listings and increase investor confidence in the South African equities market.[323] The new *JSE Listings Requirements* came into effect from 1 September 2003, with the exception of certain transitional provisions, which became effective from 1 January 2004. These new requirements accommodate certain provisions of *King Report on Corporate Governance*, take precedence over any other legal requirements or dispensations and apply equally to companies listed on the JSE.[324]

---

[319] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 23.

[320] Rossouw G. J, van der Watt A and Malan D. P, Corporate Governance in South Africa, *Journal of Business Ethics*, (2002) Vol. 37, 289-302.

[321] Deutsche Bank Securities Inc., *Global Corporate Governance - Valuing Corporate Governance in South Africa*, (2002) 30.

[322] Ibid.

[323] Vallet *et al*, *Overview of Recent Corporate Governance Reform: South Africa,* 1.

[324] Section 3.84 of the *JSE Listings Requirements* provides that, in addition to complying with section 8.63(a) of the *JSE Listings Requirements*, listed companies must also comply with a number of specifically itemised corporate governance requirements, and must disclose their compliance therewith in their annual report. See also Deloitte, *Guide to the JSE Listings Requirements*, 6-12.

المنارة للاستشارات
www.manaraa.com

Below are discussions on some of the *JSE Listings Requirements* which have the effect of restricting directors' powers and remuneration.

2.2.5.2 Corporate Governance Related Listing Requirements

The *JSE Listings Requirements* present a number of restrictive measures on directors' powers and excessive remuneration. The *JSE Listings Requirements* provide that there must be a policy detailing the procedures for appointments to the board to ensure that the appointments are formal and transparent.[325] They also provide for changes in the composition of the board of directors and a policy that shows a clear division of responsibilities at board level to ensure a balance of power and authority, such that no one individual has the sole decision-making power.[326] To augment this, the *JSE Listings Requirements* also provide for the mandatory separation of the roles of the Chief Executive Officer and Chairman to avoid excessive power and authority.[327]

Furthermore, the *JSE Listings Requirements* provide for the appointment of audit and remuneration committees, comprising a majority of independent non-executive directors,[328] in accordance with the provisions of the *King Report*. To this effect, the definitions of what constitutes independent and non-executive directors[329] have been revised. The main idea behind having a majority of independent non-executive directors, is to enable objective and unbiased checking of directors' actions as well as provision of independent advice and guidance to executive directors.

[325] Section 3 of the *JSE Listings Requirements*. In addition, the *Listing Requirements* require that a brief CV of each director standing for election or re-election at the annual general meeting should accompany the notice of annual general meeting contained in the annual report.

[326] Section 3 of the *JSE Listings Requirements*.

[327] Ibid.

[328] The capacity of each director must be categorised as executive, non-executive or independent, using the guidelines provided in the listing requirements to determine which category is most applicable to each director.

[329] Section 3 of the *JSE Listings Requirements*. These are also defined in the *King III Report* as indicated in paragraph 2.2.2.4 above. In addition, it must be noted that any director that participates in a share incentive/option scheme will not be regarded as independent.

www.manaraa.com

In addition to complying with the above, listed companies are required to disclose in the annual report how they have applied the principles set out in the *King Report on Corporate Governance*, providing explanations that enable its shareholders to evaluate how the principles have been applied. It is also a requirement to indicate the extent of the company's compliance with the *King Report on Corporate Governance* and the reasons for non-compliance with any of the principles in the Code. It therefore, means that all listed companies are required to practice good governance as recommended by the *King Code* and if compliance with these requirements is at a high level directors' powers and remuneration should not go unchecked.

2.2.6 Remuneration of directors

2.2.6.1 Introduction

Executive pay has been subjected to greater criticism mostly due to the economic downturn combined with public resentment over the role excessive levels of remuneration have had in the fall down of the financial markets.[330] According to Mervyn King, there are three "corporate sins"[331] which directors should guard against namely sloth[332], greed[333] and fear.[334] Any director who commits any of the corporate sins abuses his powers and does not act in the interests of the company. To counteract corporate sins Emery *et al*[335] suggest that company directors must be people of integrity, people who

[330] PricewaterhouseCoopers Southern Africa, *Corporate Governance- An Executive Guide to King III,* available at www.complianceweek.com/s/documents/south-africa-report.pdf (visited on 18 August 2009).

[331] Corporate sin is defined as an intentional violation of the company's laws (Institute of Directors, *King Report on Corporate Governance, 2002).*

[332] Sloth is the unwillingness to take risks and initiatives which results in a loss of flair and enterprise and the creation of a slow-moving bureaucracy to manage the company.

[333] Greed is the desire of executive managers to get the best for themselves out of their company which leads to short-term decision-making without proper regard for the long-term future.

[334] Fear arises when executives worry about what their shareholders will say or do, so that decisions are taken that will keep shareholders content.

[335] Emery D. R, Finnerty J D and Stowe J D, *Corporate Financial Management*, 2nd Edition (Upper Saddler River 2004) 370-381.

المنارة للاستشارات
www.manaraa.com

are highly capable of efficiently running a company and they also need to have a good management tracking record. They further suggest penalties for failure to perform as expected and that rewards for surpassing targets must be clearly outlined to enforce the spirit of transparency and accountability within an organization. However, protecting investors against greedy professional directors runs the risk of sloth and fear hence the need for a proper balance within a sound system of corporate governance.[336] Corporate governance thus provides a platform by means of which corporate sins by company officials can be reduced.

It is generally accepted that directors are greatly motivated to perform their duties well if they are adequately remunerated. However, it is also important to note that a director may obtain no other benefit from his position as director than that to which he is entitled to by way of his remuneration.[337] Although shareholders do not object to high remuneration for directors, their view is that rewards should largely depend on company performance and the benefits obtained for the shareholders.[338] It is thus generally accepted that performance-related elements of remuneration should constitute a substantial portion of the total remuneration package of directors in order to align their interests with those of the shareowners.[339] In this regard, the main complaint about excessively paid directors is that when the company does well the directors are rewarded well, which is fair enough, but when the company performs badly the directors continue to be paid just as well. To enable them to assess the reasonableness of directors' remuneration, shareholders require transparency in the reporting of remuneration of directors.[340]

---

[336] Ibid.

[337] See *Robinson v Randfontein Estates Gold Mining Company Limited* 1921 (AD) 168 where it was held that a director may not make a secret profit or otherwise place himself in a position where his fiduciary duties conflict with his personal interests.

[338] Talha M, Salim A S A, Masoud S, A Study on Directors' Remuneration and Board Committee in Malaysia, (2009) 34-35.

[339] Ibid.

[340] See section 297 of the Companies Act 61 of 1973 and section 30 of the Companies Act 71 of 2008 as examples of disclosure requirements.

المنارة للاستشارات
www.manaraa.com

Worldwide, there is a focus on the need for vigorous governance processes around executive remuneration together with the requirement for transparency and accountability. These themes are supported in both the *King II* and *King III* where three general principles in respect of the remuneration of directors and senior executives are set out namely, companies should remunerate directors and executives fairly and responsibly, disclose the remuneration of each individual director and certain senior executives and shareholders should approve the company's remuneration policy.[341] These general principles aimed at limiting directors' powers in determining their own remuneration and paying themselves excessively are explained below.

2.2.6.2 King Code on Corporate Governance

2.2.6.2.1 Remuneration Committee

The *King Report* recommends that the board must, at a minimum, establish a remuneration committee which should be chaired by independent non-executive directors.[342] The idea to have the remuneration committee is to enhance the effectiveness of board of directors, in which majority of independent directors, being members of the committee, deal with specific remuneration matters independently. Membership of the remuneration committee or board committee that considers executive remuneration must be disclosed in the annual report and the chairperson of such committee should attend annual general meetings to answer any questions from shareholders.[343] The committee is responsible for making recommendations to the board on executive remuneration and assists it in setting and administering remuneration policies.[344] The committee should come up with a remuneration policy which should be aligned with the strategy of the

---

[341] Chapter 2 of the *King II* and Chapter 2 of the *King III*.

[342] Ibid.

[343] Ibid.

[344] Ibid.

المنارة للاستشارات
www.manaraa.com

company, linked to individual performance and aims to attract and retain quality directors.[345] The Remuneration policy should then be subjected to shareholders' vote before implementation.[346] These recommendations ensure that the remuneration paid to directors is subjected to some form of scrutiny and does not go unchecked.[347]

2.2.6.2.2 Disclosure of Directors' Remuneration

Companies should provide full disclosure of directors' remuneration on an individual basis.[348] Disclosure assists in achieving transparency and accountability and has the effect of deterring directors from committing acts of misconduct or receiving unscrupulous benefits which effectively reduces malpractice or excessive executive rewards. In addition disclosure brings to light any form of misconduct and noncompliance enabling shareholders and other interested people to take appropriate corrective action. As part of disclosure, listed companies should disclose emoluments, for example fees, basic salaries, bonuses, share options and performance-related payments (which should constitute a large portion of each executive's package) made to directors during the last financial period in their annual financial statements.[349] The *King III* further recommends that the remuneration reports for all companies, included in the integrated report,[350] should include the policy on base pay, the use of benchmarks,

---

[345] Section 1 of the *King II* and chapter 2 of the *King III*. In the light of the skill required for a person to become a director, the *King II Code of Corporate Practices and Conduct* provides that directors' remuneration should be sufficient to attract, retain and motivate executives of the quality required by the board. See also Vallet P, *et al*, *Overview of Recent Corporate Governance Reforms: South Africa*, 1.

[346] Chapter 2 of the *King III*.

[347] The main challenge, however, is that, despite the *King Code*'s recommendation for remuneration committees, many business entities have not bothered to put the committees in place and where they have been formed they are not functioning as effectively as they should. (Prasanna P K, *Corporate Governance and Directors Remuneration*, The Chartered Accountant May 2005 available at http://icai.org/resource_file/10641may05p1483-89.pdf. (visited on 23 July 2009)).

[348] Chapter 2 of the *King II* and Chapter 2 of the *King III Code of Corporate Practices and Conduct*.

[349] Chapter 9 of the *King II* and Chapter 9 of the *King III.*

[350] Chapter 9 of the *King III Report* outlines the reporting obligations of companies. The *King III* Report endorses the use of an integrated report, which provides that a company should engage in sustainability reporting, in terms of which the company provides an account of its economic, social and environmental impact. Integrated reporting means a holistic and integrated representation of the company's performance in terms of both its finances and its sustainability.

المنارة للاستشارات
www.manaraa.com

incentive schemes to encourage retention, justification of salaries above the median, material payments that are ex-gratia in nature and policies regarding executive employment.[351] All these recommendations, if properly implemented, should enhance transparency as well as restrain directors' powers in so far as payment of excessive salaries is concerned.

2.2.6.2.3 Shareholder Approval of Directors Remuneration

Shareholders should pass a non-binding advisory vote on the company's yearly remuneration policy and the board should determine the remuneration of executive directors in accordance with the remuneration policy put to shareholder's vote.[352] Over and above the requirement that shareholders should approve the company's remuneration policy the *King Report* recommends that shareholders should approve all other forms of remuneration to the directors. It is recommended that any share options granted to non-executive directors should be approved by shareowners, usually at the Annual General Meeting and be in accordance with the provisions of the Companies Act.[353] To curb inside trading, every listed company should prohibit share dealings in its securities by directors, officers, and other selected employees prior to the announcement of its results and during other sensitive periods having regard to the *Listings Requirements* of the JSE in respect of dealings of directors.[354]

Further to this, the re-pricing of share options should be subject to shareholder approval and full disclosure is required for each director in respect of options and other share issues. It is also recommended that non-executive directors be issued shares as part of their remuneration, rather than be granted share options to maintain their

[351] Chapter 2 of the *King II* and King *III*.

[352] Chapter 2 of the *King III*. It is important to note that only the *King III* provides for this and it was not a requirement under the *King II*.

[353] Chapter 2 of the *King II* and Chapter 2 of the *King III*. See also Clive D K, *King II Report on. Corporate Governance 2002: Summary of Code of Corporate Practices and Conduct*, available at www.rtmc.co.za/.../king%20ii%20report%20summary%20of%20code.pdf (visited on 23 June 2009).

[354] Chapter 2 of the *King III*.

المنارة للاستشارات
www.manaraa.com

independence.[355] In addition to the above, it is also recommended that an executive director's contract should not be for more than 3 years unless approval has been granted by shareholders.[356] These provisions, among others, act as restrictions on executive directors' powers in share dealings and provide for enhanced transparency.

2.2.6.3 The Companies Act

2.2.6.3.1 Introduction

Directors have no automatic right to remuneration and as such the company may only pay remuneration to its directors for their service as directors in compliance with the Memorandum of Incorporation, contracts of employment and any directions given through special resolutions by shareholders voting in company general meetings.[357] The remuneration may take various forms ranging from, *inter alia*, salaries, bonuses, performance-related payments, pension schemes, loans or financial assistance, expense allowances, share options and other non-monetary benefits.[358]

The Companies Act limits the powers of directors in so far as remuneration and certain acts are concerned as a way of avoiding payment of excessive salaries and benefits.[359] Some of the statutory provisions worth noting are restrictions on directors' taking financial advantage,[360] share dealings,[361] loans and financial assistance[362] and disclosure

---

[355] Ibid.

[356] Ibid.

[357] Section 66 of the Companies Act 71 of 2008. See also Sher H, Company Directors' Duties and Responsibilities, (2005) *Juta's Business Law, Vol* 13(3) 129.

[358] See section 297 of the Companies Act 61 of 1973 and section 30 of the Companies Act 71 of 2008 and section 8 of the *JSE Listing Requirements* for definitions of remuneration.

[359] Section 221-228 of Companies Act 61 of 1973.

[360] A director who is in any way, directly or indirectly, materially interested in contracts or proposed contracts of the company has to declare his interest, giving full particulars (sections 234(1) and 237(1) and (2) of Companies Act 61 of 1973 and section 75 of the Companies Act 71 of 2008). A director who fails to comply with this requirement commits a criminal offence punishable by a fine (section 234(4)).

المنارة للاستشارات
www.manaraa.com

in annual financial statements.[363] A few of the legal and regulatory restraints on directors' remuneration, as provided in the Companies Act, are discussed below.

2.2.6.3.2 Shareholder Approval of Remuneration

The risk of misapplication of company funds through abuse of control is addressed by provisions regulating financial assistance to holding companies and co-subsidiaries, as well as to directors of the company or of its holding company and co-subsidiaries.[364] Regulation ranges from compulsory disclosure in the case of loans directly made to holding companies and co-subsidiaries, through the requirement of shareholder approval for loans to the company's own directors after satisfaction of certain requirements,[365] to an outright ban on financial assistance to directors of holding companies and co-subsidiaries.[366] Regardless of the type of regulation involved, certain actions or omissions can render directors personally liable for the damage or loss suffered by the company.[367] As an enforcement measure, "any director or officer of a company who, with full knowledge, authorizes, permits or is a party to the making of any loan or the provision of any security contrary to the provisions of the Act, is held personally liable to compensate the company and any other person who was unaware of the

---

[361] Where directors are authorized by the articles or by any resolution to issue shares at their discretion, they may not issue such shares to themselves (or their nominees) unless certain conditions are met (section 222 of Act 61 of 1973 and sections 36-41 of the Companies Act 71 of 2008). The provisions of the Securities Services Act 36 of 2004 should also be borne in mind in the case of companies whose securities and financial instruments are dealt on a regulated market.

[362] Generally, a company may not make any loans, directly or indirectly, to a director of the company or its holding company (or a company that is a subsidiary of its holding company or any other company or body corporate controlled by one or more directors of the company, its holding company, or a company that is a subsidiary of its holding company) (s 226(1) of Companies Act 61 of 1973).

[363] The directors must cause to be prepared and lay before the annual general meeting annual financial statements which show certain minimum information (sections 284-310 of Act 61 of 1973 and section 30 of Act 71 of 2008).

[364] Section 41 & 45 of Act 71 of 2008. See also Van Der Linde K, The Personal Liability of Directors for Corporate Fault–An Exploration, (2008) 20 *South African Mercantile Law Journal* 439–461.

[365] Section 45 of the Companies Act 71 of 2008.

[366] Ibid.

[367] Section 77 of the Companies Act 71 of 2008. Van Der Linde K, The Personal Liability of Directors for Corporate Fault–An Exploration, (2008) 439-461.

المنارة للاستشارات
www.manaraa.com

contravention, against any loss directly resulting from the invalidity of such loan or security and is guilty of a criminal offence."[368]

Another restriction is on dealings in shares by directors. Even if an executive director is not a long term holder of the company's shares, he is likely to acquire shares at some time or another, through exercising share options that have been awarded as part of his remuneration package. A governance issue that arises with share dealing by directors is that directors are likely to know more about the financial position of the company than other investors. It is therefore, conceivable that some directors might take advantage of their inside knowledge to buy or sell shares in the company before information affecting the share price is released to the stock market. There are laws and regulations intended to prevent the directors from dealing in shares without the knowledge or approval of the shareholders,[369] or in such a way as to benefit from inside information prior to any formal announcement in respect of the company's financial results.[370]

2.2.6.3.3 Disclosure of Remuneration

The requirement for disclosure and approval by members is a checking mechanism that seeks to ensure that directors' power to remunerate themselves as they please are curbed. To ensure transparency and accountability, companies are expected to disclose the amount and nature of remuneration paid to directors. Section 30 of the Companies Act 71 of 2008 requires directors to disclose, in the company's financial statements, the remuneration[371] and benefits received by each director as well as details of any other

[368] Section 226(4) (*a*) of the Companies Act 61 of 1973 and section 45(7) of the Companies Act 71 of 2008.

[369] Section 41 of Act 71 of 2008 provides that shares, securities, options or rights issued to a director or future director must be approved by a special resolution of the shareholders of a company.

[370] Section 73 of the Securities Services Act 36 of 2004. Bugingo K, *The impact of Corporate Governance on Firm's Market in South Africa*, Published Msc Thesis, 2006 available at http://dspace.lib.cranfield.ac.uk/bitstream/1826/1765/1/ThesisFinalD%20Konde%20Bugingo%20MSc.pdf. (visited on 15 October 2009).

[371] In terms of section 30(6) of Act 71 of 2008 remuneration includes fees paid for services rendered as directors, basic salary, bonuses and performance related payments, expense allowances, any other material benefits received, pension scheme contributions, share options gains, financial assistance for the subscription of shares and the value of any interest deferred, waived or forgiven on a loan or other financial assistance by the company to a director or person

المنارة للاستشارات
www.manaraa.com

payment made.[372] The Act thus indicates the minimum information that is supposed to be reflected in a company's financial statements and annual report as a way of enhancing financial discipline, transparency and accountability. To encourage compliance and accurate disclosure, the Act imputes liability on a director of a company for any loss, damages or costs sustained by the company as a direct or indirect consequence of the director having signed, consented to, or authorised the publication of any financial statements that were false or misleading in a material respect.[373]

An important issue that has been established from the above is that directors need to be remunerated for the duties performed and the risks taken on behalf of the company, but the remuneration should be adequately linked to the duties so performed. Legislation, common law and corporate governance principles determine how directors should be remunerated and provide for a checking mechanism to ensure that directors are not the sole determinants of their own salaries.

2.2.6.4 JSE Listings Requirements

The *JSE Listings Requirements* also set rules and regulations to limit abuse of power by directors as far as their remuneration is concerned. With regards to granting of loans for example, the *Listings Requirements* prohibit loans made either directly or indirectly to directors unless all members give their consent, a special resolution approves a specific loan, the loan is to enable a director to perform his or her duties, the business of the company is to make loans, the loan is to provide assistance to enable the director to

---

related to him. See also sections 295-297 of Act 61 of 1973 for the definition of remuneration and disclosure requirements.

[372] Shareholders can also make use of the provisions of the Promotion of Access to Information Act 2 of 2000 to request for more details as long as the information so requested is not in violation of the provisions of the Act and any other relevant Act.

[373] Section 77(3)(d)(i) of the Companies Act 71 of 2008 and section 287A of the Companies Act 61 of 1973. On the other hand, the rules governing insurance and indemnities that companies may take out or provide for the benefit of their directors have been clarified in the New Act and create scope for increased protection against the consequences of mere negligence on the part of directors.

المنارة للاستشارات
www.manaraa.com

participate in a company's share incentive scheme or the loan is for director's housing.[374]

While the Companies Act itself mandates certain standards of information disclosure, *JSE Listings Requirements* have substantially added to these requirements in an attempt to make the information disclosed in companies' records for example the prospectus and annual accounts more meaningful and to enhance transparency.[375] In line with the international trend of moving from disclosure on an aggregate basis to individualized disclosure of remuneration, the JSE now requires listed companies to disclose directors' compensation,[376] as required by the Companies Act, on an individualized basis.[377] The *JSE Listings Requirements* have further expanded the current understanding of what should be disclosed with regard to the directors' emoluments to include amounts received from the issuer's holding company, subsidiaries, fellow subsidiaries, associates, joint ventures and any entity that provides any management or advisory services to such entities as well as management, consulting and other such fees whether paid directly to a director or to a management company where part of that fee is then paid to a director.[378] This should significantly enhance transparency and independence as well as instill discipline and responsibility in directors for fear of public scrutiny and disqualification as a director.

To further enhance transparency, the *JSE Listings Requirements* make it mandatory that there be full disclosure of details of the individual directors such as names, business address, nationalities, qualifications and experience, other directorships or partnerships

---

[374] Section 5 of *JSE Listings Requirements.* See also Grant Thornton South Africa, *JSE Listings Requirements*, available at http://www.gt.co.za/Publications/Effective-directors-guide/jse.asp (visited on 20 August 2009).

[375] Section 3 of *JSE Listings Requirements.* See also Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, (2008) 72-75.

[376] This should include fees for services, basic salary, bonuses and performance related payments, expense allowances, any other material benefits received, pension scheme contributions, any commission, gain or profit sharing arrangements, any share options and fees paid to a third party in lieu of directors fees.

[377] See section 8 of the *JSE Listings Requirements*.

[378] Ibid. See also Deloitte, *Guide to the JSE Listings Requirements*, 33.

المنارة للاستشارات
www.manaraa.com

and questions which relate to integrity and the directors' previous “track record” as a director of companies.[379] A listed company is also required to provide the JSE with full details of transactions in the company’s securities or property by or on behalf of a director (whether held directly or indirectly, beneficially or non-beneficially, including immediate family members).[380] In addition, executive directors may not be appointed as trustees of share schemes but non-executive directors may be appointed as trustees provided they do not benefit from the share scheme.[381] All these efforts are targeted towards enhancing transparency, discipline and accountability thus promote good corporate governance.

2.2.7 Enforcement Mechanisms

2.2.7.1 King Code

South Africa has relied on a self-regulation[382] environment in its approach to corporate governance, as evidenced in the “comply-or-explain” provision regarding the *King I* and *II* and “apply or explain” provision in the *King III*.[383] What this means is that, while the *King Codes* set out the basic requirements on corporate governance, they have not been given the force of an Act of Parliament. Nonetheless, the Codes have had an impact on how companies should be and are managed and evaluated[384] partly because of mere voluntary compliance by companies and partly because enforcement of the *King Codes* recommendations is effected by the Johannesburg Securities Exchange which makes

[379] See section 7 and schedule 21 of the *JSE Listings Requirements*.

[380] Ibid section 3.

[381] Ibid section 14.

[382] See *Minister of Water Affairs and Forestry V Stilfontein Gold Mining Co Ltd and Others* where the court referred extensively to the second *King Report* to determine if the directors had breached their duties. The case highlights the fact that, although the *King Report’s* recommendations are not mandatory they are influential and can be used as a test to determine whether directors observed their fiduciary and statutory duties.

[383] PricewaterhouseCoopers (PwC), *Corporate Governance in South Africa: A Comparison of the King Report 2002 and the Sarbanes-Oxley Act of 2002,* 6-13.

[384] Institute of International Finance, *Corporate Governance in South Africa-An Investor Perspective*, September 2007. (IIF 2007) at http://www.iif.com/download.php?id=0N6SZ+azhm0= (visited on 27 May 2009). See Footnote 380.

المنارة للاستشارات
www.manaraa.com

acceptance of the Codes one of the Exchange's *Listing Requirements* as well as through other statutes particularly the Companies Act.[385]

It is important to appreciate that legislative corporate governance codes do not necessarily mean compliance as voluntary self regulation may be more effective in certain circumstances. PricewaterhouseCoopers Southern Africa has said in support of self-regulation:

> "*It can be convincingly argued that self-regulation, in which an organisation voluntarily monitors its own adherence to legal and ethical standards, is far preferable to having an outside agency such as government monitor and enforce those standards. This approach allows organisations to maintain control over the standards to which they are held by successfully self-policing themselves. Apart from the bureaucratic burden that would be imposed by external enforcement, the cost of setting up such a mechanism is also avoided.*"[386]

However, it would be unrealistic to anticipate that the *King Report* on its own, given the voluntary nature of compliance with its recommendations, would generate an absolute transformation in corporate governance standards and practices in South Africa. It is thus acknowledged that other interventions are necessary to create the climate necessary to ensure adherence to these guidelines hence the promulgation of the Companies Act 71 of 2008 and the revision of the *JSE Listing Requirements*, among others.

---

[385] Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 108. Various elements of the recommendations in the second *King Report* have also been incorporated into legislation and regulations relating to financial markets to ensure that directors practice good corporate governance.

[386] Pricewaterhousecoopers Southern Africa, *Corporate Governance – Executive Guide to King III*, September 2009, 2.

المنارة للاستشارات
www.manaraa.com

2.2.7.2 The Companies Act

A number of consequences flow from directors' failure to meet or fulfil their duties to the company under the 1973 Companies Act,[387] various statutes, the common law,[388] and Companies Act 71 of 2008.[389] Under the Companies Act 71 of 2008, where a director breaches the section/(s) which contain directors' duties, such director will incur civil and/or criminal liability.[390] Criminal liability can arise, under the Companies Act, where it is commonly used to encourage directors to ensure that their companies comply with formalities, under various other statutes.[391] Civil liability can be incurred, among other things, in relation to fraudulent or reckless trading,[392] unlawful distributions to shareholders,[393] investor protection,[394] and loans to directors or controlling companies.[395] The Companies Act 71 of 2008 further provides for liability of directors where they seek to obstruct justice.[396] The penalties for wrongful acts by directors range from a fine to a

[387] Sections 234-241 of the Companies Act 61 of 1973.

[388] *Du Plessis NO v Phelps* 1995 (4) SA 165 (C) at 170*; Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W) at 166*; Re Brazilian Rubber Plantations and Estates Ltd* [1911] 1 Ch 425 (CA) at 437*; Re D'Jan of London Ltd Copp v D'Jan* 1994 1 BCLC at 561.

[389] Section 77 of the Companies Act 71 of 2008.

[390] Liability could be imposed on the basis that the director authorised, permitted or was a party to the contravention, was knowingly a party to the contravention, knowingly contravened or permitted a contravention, failed to take reasonable steps to prevent a contravention or issued, signed or authorised the issue or signing of certain documents. The 1973 Companies Act relied broadly on criminal sanctions to enforce compliance with its provisions but the New Act aims to decriminalise company law as criminal sanctions are not deterrent enough if they are not effectively enforced. To discourage gross mismanagement and abuse of power and to minimize on the expense and the lengthy period it takes to litigate in criminal matters, the Companies Act 71 of 2008 has provided for private-law remedies. An example of the remedies is that directed at directors who have deliberately abused their positions. In this regard the court has the powers to disqualify such directors from serving as directors or to place them on probation (section 162). Likewise a member is also empowered to bring proceedings on behalf of the company where the company has been prejudiced because of the directors' abuse of power and the same directors have not been called to account for their actions (section 163).

[391] A number of other Acts imposes personal or criminal liability on directors for wrongful acts for example the Labour Relations Act 66 of 1995, Employment Equity Act 55 of 1998, National Environmental Management Act 107 of 1998 and the Unemployment Insurance Contributions Act 4 of 2002 to mention just but a few.

[392] Section 22 of the Companies Act 71 of 2008. See also section 424 of the Companies Act 61 of 1973.

[393] Section 66 of the Companies Act 71 of 2008.

[394] Sections 58-65 of the Companies Act 71 of 2008.

[395] Section 45 of the Companies Act 71 of 2008.

[396] Sections 29 of the Companies Act 71 of 2008 makes directors and officers liable for are materially false or misleading statements and evidence and for falsification of books and records. This has a deterrent effect especially where directors have to disclose certain information for example their remuneration. Furthermore, section 332 of the

المنارة للاستشارات
www.manaraa.com

maximum period of ten years depending on the nature of the offence.[397] The penalties are deterrent enough to inhibit any director who might be contemplating to violate the provisions of the Act.

Under the common law, where a director breaches his fiduciary duties toward the company, such director will be liable for loss arising from such breach, where a director breaches his duty to the company to take reasonable care and skill in the management of the company's affairs,[398] such director will incur delictual liability and where a director is guilty of an offence, such director may incur criminal liability under the common law principles of accessory criminal liability.[399] Enforcement of these duties is by means of a derivative action either at common law or in terms of the Companies Act. The Companies Act 71 of 2008 abolishes the common law derivative action and makes the statutory derivative action exhaustive.[400]

Under the 1973 Companies Act and the common law, the derivative action could only be instituted by shareholders.[401] In contrast, under section 165 of the Companies Act 71 of 2008, the derivative action may be brought by a shareholder or a person entitled to be registered as a shareholder of the company or of a related company, a director or prescribed officer of the company or of a related company, a registered trade union that represents employees of the company, or another representative of employees of the

---

Criminal Procedure Act 51 of 1997 provides for criminal liability of a company director or officer in the exercise of the person's authority.

[397] Section 216 of the Companies Act 71 of 2008.

[398] See paragraph 2.1.3 above.

[399] In support of this view, section 158 of the Companies Act 71 of 2008 provides that "when determining a matter brought before it in terms of this Act, or making an order contemplated in this Act a court must develop the common law as necessary to improve the realization and enjoyment of rights established by this Act". See also Van Der Linde K, The Personal Liability of Directors for Corporate Fault–An Exploration, (2008) 439-461.

[400] Section 165 of the Companies Act 71 of 2008.

[401] The common law derivative action presented challenges in that the member could personally incur legal costs and had to launch the proceedings while the required information was held by the company and offenders (Davies D *et al, Companies and Other Business Structures in South Africa*, (2009) 187-188.

المنارة للاستشارات
www.manaraa.com

company; and a person who has been granted leave of the court.[402] The Companies Act 71 of 2008 thus retains the statutory derivative action, but with significant modifications aimed at making it more effectual.[403]

In addition to the enforcement mechanisms discussed above, the Companies Act provides for the removal of directors[404] who are considered unfit to serve as directors as well as for the disqualification of the directors[405] and for a register of disqualified directors to be maintained by the registrar of companies.[406] This ensures that unsuitable individuals are not allowed to manage the company's affairs thus protecting the investors and other stakeholders' interests. It has however, been argued that disqualifying and declaring directors delinquent would amount to blacklisting individuals and would discourage people from taking on directorship. On the other end, some commentators argue that the potential for disqualification is likely to act as a checking mechanism and deterrence on would be fraudulent directors.[407]

Furthermore, the power of the Minister in terms of section 258(2) of the Companies Act 61 of 1973 to appoint inspectors to investigate the affairs of a company and to report is also an important regulatory mechanism for ensuring probity in the management of companies' affairs so that they are properly managed. Likewise, the provision in the

[402] The leave may be granted only if the court is satisfied that it is necessary or expedient to grant such leave to protect a legal right of such person.

[403] Section 165 of the Companies Act 71 of 2008. See also Davies D *et al, Companies and Other Business Structures in South Africa*, (2009) 187-188.

[404] Section 220 of Act 61 of 1973 and section 71 of the Companies Act 71 of 2008. A director can be removed by shareholders and in some instances, by the board of directors.

[405] Section 162 of the Companies Act 71 of 2008 provides for one to be declared a delinquent director if the person while a director grossly abused the position of director, did not declare his personal interest in a contract, "intentionally, or by gross negligence, inflicted harm upon the company or a subsidiary of the company," and acted in a manner "that amounted to gross negligence, wilful misconduct or breach of trust in relation to the performance of the director's functions".

[406] Section 69 of the Companies Act 71 of 2008.

[407] The conditions set in section 162 are so harsh and should significantly deter directors from breaching their duties. The disqualification subsists for a period of seven years from the date of the order, or such longer period as determined by the court at the time of making the declaration. The punishment can even subsist for the lifetime of the person declared delinquent depending on the nature of the offence.

المنارة للاستشارات
www.manaraa.com

Companies Act 71 of 2008 for the protection of whistleblowers[408] should go a long way to encourage people to disclose information regarding breach of duty by the directors or other officers of the company without fear of liability for such disclosure.[409] To add to the above, the Companies Act 71 of 2008 [410] makes provision for a new institutional framework consisting of a Companies and Intellectual Property Commission aimed at ensuring proper administration, compliance with, and enforcement of the provisions of the Companies Act.[411]

It can therefore, be safely concluded that, although directors may exercise all the powers of the company these powers are subjected to some legal and regulatory restraints as a way of ensuring that the interests of shareholders and other stakeholders are sufficiently satisfied. A number of regulatory provisions ranging from compulsory disclosure in the case of directors' remuneration and other information in financial statements and annual reports, the requirement of shareholder approvals before certain things are done and personal liability for wrongful acts and stiff penalties have been set in the Companies Act as a way of enforcing compliance by directors. The enhanced protection of whistleblowers and the setting up of a Companies and Intellectual Property Commission should also go a long way in regulating the conduct of directors. All these efforts are aimed at encouraging directors to carry out their fiduciary duties diligently, ensure that their companies comply with the relevant laws and engage in good corporate governance practices.

[408] Section 159.

[409] A whistleblower, who makes a disclosure contemplated in terms of section 159 has qualified privilege in respect of the disclosure and is immune from any civil, criminal or administrative liability for that disclosure. See also section 2 of the Protected Disclosure Act 26 of 2000.

[410] Section 185 of the Companies Act 71 of 2008.

[411] Sections 185-188 of the Companies Act 71 of 2008. The Commission must promote proper compliance with the Act, receive and promptly investigate complaints concerning violations of the provisions of the Act, encourage the use of Alternative Dispute Resolution by companies for resolving internal disputes and issue and enforce compliance notices (section 187(2)).

المنارة للاستشارات
www.manaraa.com

2.2.7.3 JSE Listing Requirements

By virtue of the fact that listed companies are required to comply with specifically itemised corporate governance requirements,[412] certain consequences follow where a listed company does not comply. In terms of section 1 of the *JSE Listings Requirements*, the JSE has the power, subject to the *Listings Requirements*, to grant, review, suspend or terminate a listing of securities or impose a fine on a listed company. Therefore, in the event that a listed company does not comply with such specifically itemised corporate governance requirements, the JSE would have the power to suspend or terminate such company's listing of its securities if it is in the public interest to do so or impose a fine on such listed company.[413]

The JSE may also publicly or privately censure the company or its directors, individually or jointly, disqualify a director from holding the office of a director of a listed company for any period of time, order the payment of compensation to any person prejudiced by the contravention or failure and thereafter may impose a penalty of up to R5 million on the company or its directors, individually or jointly.[414] The JSE may also, in its discretion and in such manner as it may deem fit, notify the public of any fact that the JSE considers to be in the public interest, including, but not limited to, the name of the member or employee of a member who has been found guilty of any charge and of the sentence imposed on such person.[415] As a further deterrent measure, the Securities

[412] Section 3 of the *JSE Listings Requirements*.

[413] Section 1 of the *JSE Listings Requirements*.

[414] Ibid. Grant Thornton South Africa, *JSE Listings Requirements*, available at http://www.gt.co.za/Publications/Effective-directors-guide/jse.asp (visited on 20 August 2009). See also section 1 of the JSE Listing Requirements.

[415] Section 1 of the *JSE Listing Requirements*. This should significantly deter would be defaulters who might not want to tarnish their images.

المنارة للاستشارات
www.manaraa.com

Services Act[416] increases significantly criminal penalties for wrongful conducts, to a fine not exceeding R50 million and imprisonment for a period not exceeding 10 years.[417]

From the above, it is clear that the *JSE Listings Requirements* and incorporation of some *King Report* recommendations into statutory law add an important legal dimension to adherence to good corporate governance standards in South Africa. The *JSE Listings Requirements* make it mandatory for companies and directors to observe certain corporate governance principles as enshrined in the *King Report* which positively impacts on the way directors conduct company business as they are forced to practice good corporate governance to attract investment and be rated highly amongst other reputable companies. In particular, the requirements also provide a strong regulatory framework in so far as directors' powers and remuneration are concerned given that failure to adhere to the *JSE Listings Requirements* is an offence which attracts stiff penalties and may result in a termination of a listing and personal liability of directors.

2.2.7.4 Regulatory Bodies

The first body to be actively involved in the promotion of corporate governance in South Africa was the Institute of Directors of South Africa (IOD). The Institute of Directors has played an integral role in the development of all the *King Reports* (*I-III*) and, in 2001, it established the Center for Directorship and Corporate Governance, which disseminates information on corporate governance trends around the world as well as provides technical training on directorship and board effectiveness.

In addition to the Institute of Directors of South Africa and the JSE discussed above,[418] South African policy-makers have put in place a wide variety of other regulatory bodies

[416] Act 36 of 2004. Aspiring to international "best practice", the Act aims to increase confidence in South African financial markets, promote the protection of regulated persons and clients, reduce systemic risk and promote the international competitiveness of securities services in South Africa.

[417] Müller N, Financial Services Board Report (2005) available at ftp://ftp.fsb.co.za/public/documents/AReport08_2005.pdf (visited on 15 May 2009).

[418] See paragraph 2.2.7.3 above.

المنارة للاستشارات
www.manaraa.com

and offices which play important supervisory, regulatory and advisory roles. The key government/securities regulators are the Minister of Trade and Industry, the Registrar of Companies, the Financial Reporting Standards Council, the Financial Services Board, the Accounting Standards Board (ASB), the Public Accountants and Auditors Board, the Securities Regulation Panel, the Competition Commission and the Exchange Control Department of the South African Reserve Bank.[419]

The Department of Trade and Industry (DTI) is responsible for the supervision of compliance with company law.[420] The Registrar of Companies, who is appointed by the Minister,[421] is responsible for the administration of the Companies Registration Office. The Financial Reporting Standards Council (the "FRSC")[422], is tasked with establishing uniform financial reporting standards for companies and will assume the role of an advisory committee to the Minister and will "advise on regulations establishing financial reporting standards, which will govern the form, content and maintenance of companies' financial records and statements";[423] The Financial Services Board[424] oversees the South African Non-Banking Financial Services Industry in the public interest and administers and ensures compliance with the securities law in order to promote and improve the efficiency of financial institutions.

The Accounting Standards Board (ASB), established by the Public Finance Management Act (1999) is responsible for approving South African accounting standards; it sets standards and guidelines for financial statements as mandated by the Constitution (1996)

---

[419] It is also important to note that South African law has also addressed corporate governance issues by, *inter alia,* ratifying a number of international conventions for example the International Convention on Economic, Social and Cultural Rights (ICESCR).

[420] New Partnership for Africa's Development (NEPAD), *African Peer Review Mechanism: Country Review Report of South Africa,* September 2007, 9.

[421] Section 7 of the Companies Act 61 of 1973.

[422] FRSC was established in terms of section 440P of the Companies Act 61 of 1973.

[423] Sections 3-9 of the Memorandum on the Objects of the Companies Act 71 of 2008.

[424] Established in terms of section 82 of the Securities Services Act 36 of 2004.

المنارة للاستشارات
www.manaraa.com

and makes recommendations to the Minister of Finance. The Public Accountants and Auditors Board[425] is the statutory body controlling that part of the accountancy profession involved with public accountancy in South Africa. The Securities Regulation Panel[426] is tasked with supervising dealings in securities and regulating all transactions or schemes which constitute "affected transactions"[427] and schemes, and all proposals which on successful completion or implementation would be affected transactions.

The Competition Commission[428] is responsible for the investigation, control and evaluation of restrictive business practices, abuse of dominant positions and mergers. The Exchange Control Department of the South African Reserve Bank administers and controls exchange control in South Africa as well as undertakes supervisory and advisory responsibilities in the regulation of the banking sector.[429] Furthermore, the Companies Act 71 of 2008 provides for the setting up of a Companies and Intellectual Property Commission[430] which will monitor proper compliance with the Companies Act and ensure that contraventions of the Act are promptly and properly investigated. All these regulatory bodies seek to enforce good corporate governance by monitoring and advising companies and directors to ensure that they are compliant with rules and regulations applicable to them.

---

[425] Established in terms of the Public Accountants' and Auditors' Act 80 of 1991.

[426] Established pursuant to Chapter XVA of the Companies Act. In the New Companies Act the Securities Regulation Panel will be substituted with the Takeover Regulation Panel, an independent organ of state, vested with the same powers and functions of the Panel.

[427] In terms of section 440 of the Companies Act, the term "affected transaction" means a transaction which is part of a series of transactions which, taking into account any securities held before such transaction, has or will have the effect of vesting control of any company in any person or two or more persons acting in concert in whom control did not vest prior to such transaction or which has the effect of such person or persons acquiring all the securities of that company, or all the securities of a particular class.

[428] Established in terms of section 79 of the Competition Act 89 of 1998.

[429] New Partnership for Africa's Development (NEPAD), *African Peer Review Mechanism: Country Review Report of South Africa,* September 2007, 12-14. However, it is important to note that the Minister of Finance has final authority in financial regulation.

[430] Section 185 of the Companies Act 71 of 2008.

المنارة للاستشارات
www.manaraa.com

2.2.8 Conclusion

South Africa has made substantial strides in promoting good corporate governance practices through both regulatory and self-regulating frameworks. Corporate governance was formally introduced by *King I Report* in 1994 and since then continuous efforts have been made to enhance corporate governance practices as evidenced by the revision of the *King Reports*. The *King Reports* have substantially contributed to the regulation of directors' conduct as a way of restricting their powers and excessive remuneration. The *Reports* have recommended that, among others, the composition and functions of the board be properly balanced, the position of chairman and chief executive officer be separated, there be audit, nomination and remuneration committees, directors' remuneration be disclosed and that shareholders be allowed to participate in company business to a certain extent.

The main idea behind all these recommendations is to ensure that there is sufficient division of power, transparency, discipline, responsibility and accountability in company management. The challenge, however, in creating a fully working corporate governance environment still lies in compliance of companies and enforcement of the standards.[431] Despite the challenges, it is also important to note that some statutory institutions such as the JSE require that their members comply with[432] and subscribe to the recommendations of the *King Report,* which in a way makes it mandatory for companies to comply with the provisions of the *King Report*. In addition to the *King Report* recommendations, the *JSE Listings Requirements* also provide for checking mechanisms on directors' powers and remuneration which if not observed may result in personal liability of directors.

On the other hand, the Companies Act also provides a regulatory approach to corporate governance and thus substantially contributes to South Africa's efforts to conform to

[431] New Partnership for Africa's Development (NEPAD), *African Peer Review Mechanism: Country Review Report of South Africa*, September 2007, 7-9.

[432] See paragraph 2.2.7.3 above for consequences of failing to comply with the *JSE Listings Requirements*.

المنارة للاستشارات
www.manaraa.com

internationally accepted corporate governance practices. The directors are obliged to carry out their obligations within the confines of the Companies Act and failure to do so results in personal liability towards the company and other interested stakeholders. A number of provisions in both the 1973 Companies Act and the 2008 Companies Act have a deterrent effect on would be delinquent directors and a restrictive effect on the abuse of powers by directors and payment of excessive remuneration to the same. A number of other statutes also place obligations on directors which they are expected to comply with or risk being held accountable and penalised.

The number of statutory and regulatory mechanisms put in place by the South African policy-makers is a clear indication that corporate governance has been identified as key to attracting foreign investment and promoting economic growth. The same efforts put by the policy makers have significantly contributed to the restricting of directors' powers and remuneration.[433] This has, in turn, had a positive impact on South Africa's credibility to its international standing and is likely to attract investment into the country and other corporate governance related benefits.

In the next chapter an assessment of the effectiveness of the statutory and regulatory mechanisms (discussed above) in promoting corporate governance in so far as directors' powers and remuneration is concerned is made. Recommendations on how the effectiveness of the statutory and regulatory mechanisms can be improved are made in paragraph 5.4.

---

[433] An assessment of whether the legal and regulatory framework is sufficient to restrain directors' powers and regulate their remuneration is made in chapter 3 below and recommendations to improve the effectiveness are made in paragraph 5.4.

المنارة للاستشارات
www.manaraa.com

CHAPTER 3

EVALUATION OF SOUTH AFRICAN CORPORATE GOVERNANCE MECHANISMS ON DIRECTORS' POWERS AND REMUNERATION

3.1 Introduction

South African listed companies are at present ranked by "foreign institutional investors as among the best governed in the world's emerging economies."[434] This is mostly because of the significant impact that the *King Report* has had on corporate governance in South Africa. The strong impact the *King Report* has had is confirmed by the number of the South African companies that genuinely practice good corporate governance.[435] Nevertheless, because of the voluntary nature of compliance with its recommendations it is acknowledged that other interventions have been considered necessary to create an environment capable of securing adherence to these guidelines.[436] South Africa has thus come up with a number of rigorous laws and regulations, as shown in chapter 2 above, which if both private companies and public sector enterprises adhere to, the country can take pride in having successfully implemented good corporate governance practices.[437] The challenge, however, is that the country has continued to experience high-profile

---

[434] Introduction and Background to the *King III Code*.

[435] According to Deutsche Bank Securities Incorporated survey conducted in 2002 a number of companies practiced good corporate governance with Gold Fields, SAB, BHP Billiton, and Sasol comprising the top tier and setting the corporate governance standard for South Africa. These companies showed strong corporate governance performances across the board. According to the survey Gold Fields, in particular, stood above the rest in all categories, namely shareholder treatment, board independence, information disclosure, and best business practices. The survey results revealed Gold Fields to genuinely embrace good corporate governance and to be the standard-bearer for corporate governance in South Africa. It is also important to note that, with the exception of Sasol, all of these companies maintain listings on the London Stock Exchange, which imposes some of the toughest corporate governance standards in the world. Such listings may partly explain the tremendous efforts these companies have made to achieve good corporate governance.

[436] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 22-23.

[437] Langtry S, *Corporate Governance, (*2005) 15.

www.manaraa.com

corporate collapses despite the existence of corporate governance codes, stringent Companies Act and *JSE Listings Requirements* and government regulation.[438]

Given the above challenges, this chapter seeks to evaluate whether the corporate governance provisions in the *King Report*, Companies Act and the *JSE Listings Requirements*, discussed in chapter 2, are sufficient to achieve good corporate governance generally and in so far as directors' powers and remuneration are concerned. It, therefore seeks to assess the effectiveness of the South African corporate governance rules and regulations and understand why, despite the existence of a number of legal and regulatory measures, directors continue to abuse their powers and enjoy excessive remuneration.

3.2 Assessment of effectiveness of corporate governance framework

Although South Africa is counted amongst the best promoters of good corporate governance in emerging economies, the compliance results have not been as pleasing as desired mostly due to a number of challenges some of which are discussed below.

3.2.1 Weak Enforcement and Prosecution

It is a commonly acknowledged proposition that at the foundation of good governance "is a predictable, equitable, effective, and efficient legal and judicial system."[439] Consequently, a deficit in the Rule of Law directly affects corporate governance. Despite the fact that South Africa acknowledges this proposition as a country, it has not been spared from the challenge that the public have not been able to rely on the law essentially because the law as written and the law as enforced in the courts can differ

---

[438] Horn R F, *The Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 49-60. The corporate scandal involving the Fidentia Group (2007) indicates that despite the existence of *King II Report* and other regulatory measures which improved regulation of corporate governance, problems are still evident.

[439] Cooper M. S, *Corporate Governance In Developing Countries: Shortcomings, Challenges & Impact on Credit,* Paper presented at the Congress to celebrate the fortieth annual session of UNCITRAL Vienna, 9-12 July 2007, available at www.uncitral.org/pdf/english/congress/Cooper_S_rev.pdf (visited on 6 January 2010).

المنارة للاستشارات
www.manaraa.com

considerably.[440] According to Falkena and others, the rate at which institutional change has taken place in South Africa has been so fast that the regulatory and supervisory authorities at times had challenges in keeping pace with appropriate regulatory changes.[441]

On the other hand, from an international investor's perspective, the main cause of concern has been the length of time that it has taken to investigate and prosecute cases of corporate mismanagement.[442] The directors who have been responsible for corporate collapses through misconduct and excessive remuneration have not been punished adequately in the eyes of the public considering the gravity of the offences committed. The cases where a director has been subject to legal action have also been very few in number and taken long to prosecute to the dissatisfaction of the stakeholders and public in general.[443] The existence of enforcement and implementation gaps thus undermines the usefulness of legal provisions and diminishes the confidence of foreign investors in the legal system as a whole.[444]

The King Committee made the following observation regarding compliance and enforcement:

> "*all principles embodied in a code of corporate governance are effective only if adequate remedies and sanctions exist to enforce compliance with those principles.*"[445]

---

[440] Cahn N, *Corporate Governance Divergence And Sub-Saharan Africa: Lessons From Out Here In The Fields,* available at justice.law.stetson.edu/lawrev/abstracts/PDF/33-3Cahn.pdf (visited on 12 June 2009*).*

[441] Falkena H, Bamber R, Llewellyn D and Store T, Financial Regulation in South Africa, *SA Financial Sector Forum,* (2001), available at http://www.finforum.co.za/publications/fregall.pdf (visited on 12 November 2009).

[442] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2000) 26-28.

[443] Davies D *et al*, *Companies and Other Business Structures in South Africa*, (2009) 185-191. According to Department of Trade Industry's general notice entitled "*South African Company Law for the 21st Century: Guidelines for Corporate Law Reform*" the most noteworthy weakness in the law before the new Act was that South African company law did not offer efficient methods for the enforcement of directors' duties prescribed under the 1973 Companies Act. This resulted in directors and senior management of large companies being "effectively immune from legal control, except perhaps in regard to the more outrageous criminal offences".

[444] La Porta R, Lopez-de Silanes F, Shleifer A and Vishny R, Investor Protection and Corporate Valuation, (2002) *Journal of Finance* 57(3) 1147-1170.

[445] Introduction and Background to the *King III Report*.

المنارة للاستشارات
www.manaraa.com

What this means is that rules are only as effective as their enforcement.[446] This makes the structure and capacity of regulatory and judicial frameworks essential parts of the corporate governance environment.[447] The gap between the written legal and regulatory provisions and actual implementation should therefore not be too wide.

Although weak enforcement of rules and regulations has been sighted as a major problem in discussions concerning South Africa, the main reason for the negative perception is not so much a general lack of enforcement, as might be the case in other emerging markets, but erratic enforcement in that in some areas it is of a high standard, but in others it is almost absent.[448] While the legislation in place is strong even when compared to some developed countries, one of the reasons for the fragmented nature of South Africa's regulatory system are the high costs that effective regulation would entail, the need to equally give significant financial priority to other important areas such as housing, health, social welfare and education, among others and also the need to meet all its international obligations[449] and establish itself as a market of integrity.[450]

Furthermore, the judicial system struggles with backlogs and is often unable to adjudicate cases quickly due to, *inter alia*, inadequate physical infrastructure, malfunctioning judicial systems, outdated laws (both procedural and substantive) and poor terms and conditions of service for judicial and related administrative personnel.[451]

---

[446] Horn R F, *The Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 150-164. Although enforcement can affect the overall credibility of a regulatory system as it both deters bad actors and levels the competitive playing field, it is important to recognise the fact that greater enforcement is not always better, for if taken too far it can dampen valuable risk-taking.

[447] Jesover F & Kirkpatrick G, The Revised OECD Principles of Corporate Governance and their Relevance to Non-OECD Countries, *Corporate Governance: An International Review*, (2005) Vol 13 (2) 127-136.

[448] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2000) 26-28.

[449] South Africa is a member of international and regional organizations such as World Trade Organisation (WTO) and Southern African Development Community (SADC) where it is expected to carry out certain obligations in terms of multilateral agreements. It is worth noting that the membership to such organisations has also added further emphasis to the need for higher standards of corporate governance in South Africa.

[450] Ibid.

[451] Deutsche Bank Securities Inc., Global Corporate Governance, *Valuing Corporate Governance in South Africa*, (2002) 31. Public services are unevenly provided and of poor quality and civil servants are often so poorly paid that they resort to petty corruption in order to survive.

المنارة للاستشارات
www.manaraa.com

Other contributory factors are "weak accountability mechanisms including, and sometimes reflected in, ineffective service by securities regulators and banking supervisory regulators and failure of law enforcement and prosecutorial authorities to pursue claims arising from violations of securities or other financial laws or white collar abuses and crimes, weak auditing and disclosure laws".[452]

To add to the above challenges, where rules and regulations exist, they occasionally provide loopholes and are often not effective, partly due to poor monitoring and oversight mechanisms and partly due to weak enforcement mechanisms.[453] If one considers financial disclosure as an example it is clear that non-compliance by public officials, across legislatures, executive institutions and the civil service is a serious problem because public officials are not motivated to submit their records timeously.[454] This is because the officials have realised that that their forms are hardly ever examined to detect noncompliance, disciplinary measures are rarely enforced and that serial offenders are not being dealt with harshly despite the range of penalties that exist.[455] This scenario is equally applicable to company directors whose actions can go unchecked and when they are discovered the penalties imposed are not prohibitive enough. However, the actual concern here is not of non-compliance as such, but rather that various officers across government are unable or unwilling, to employ punitive measures to reprimand those who willingly disown their duty to remain publicly accountable.[456]

---

[452] Cooper M. S, *Corporate Governance in Developing Countries: Shortcomings, Challenges & Impact on Credit,* (2007) 3.

[453] Rossouw *et al*, *Corporate Governance in South Africa*, (2002) 289-302. According to the Department of Trade Industry's general notice, "*South African Company Law for the 21st Century: Guidelines for Corporate Law Reform,*" "the lack of enforcement and recourse is in part attributable to the disincentives to ligation created by the court system, such as the underdeveloped nature of class actions and contingency fees and the costs of protracted litigation, which collectively diminish the effectiveness of the civil and criminal sanctions and remedies contained in the law".

[454] Institute for Security Studies, *Why Ethics Regulations Continue to Fail SA,* available at http://www.polity.org.za/article/why-ethics-regulations-continue-to-fail-sa-2009-09-02, (visited on 20 Sept 2009).

[455] Ibid.

[456] Ibid. The South African Public Service Commission reported a 48% compliance rate among senior managers in the public service in 2008 and recommended that non-complying members be charged with misconduct but this was not implemented.

المنارة للاستشارات
www.manaraa.com

The other challenge experienced by South Africa is that it has relied on a self-regulation environment in its approach to corporate governance, as confirmed in the "comply-or-explain" provision regarding the *King Code I* and *II* and "apply or explain " provision in the *King Code III*.[457] However, this does not mean that self-regulation does not have its advantages, but the only challenge is that directors just "box-tick" without actual complying with the corporate governance principles.[458] Research has shown that whilst most listed companies in South Africa view corporate governance as an important matter, full compliance with the *King Corporate Governance Code* is still rare and a substantial number of companies comply only with the letter, and not the spirit of the code.[459] For example, many companies do not provide adequate information about their companies' internal operations, such as how directors are evaluated or how much each director is remunerated.[460]

What the above points out to is that, whilst laws and regulations are necessary they are not adequate on their own. There is need for strong commitment from the human actors, that is directors in this case, who must comply with the relevant rules and regulations as even the most stringent corporate governance standards may be inadequate to curb complex fraud and other corrupt tendencies.[461] It has been noted that the failure of Enron had little to do with insufficient corporate governance standards and procedures, but everything to do with the culture, environment and conduct of the people at Enron.[462]

---

[457] PricewaterhouseCoopers (PwC), *Corporate Governance in South Africa: A Comparison of the King Report 2002 and The Sarbanes-Oxley Act of 2002*, (2002) 6-10.

[458] According to King, even with the "comply or explain" regime directors just "box-tick" to avoid having to go through the cumbersome process of explaining non-compliance (King M, *Governance for All Entities,* (2006) 12). See also KPMG, Survey of Integrated Sustainability Reporting in South Africa, (Johannesburg 2006) 19-23.

[459] Deutsche Bank Securities Incorporated, *Global Corporate Governance*, *Valuing Corporate Governance in South Africa*, (2002) 27.

[460] Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, (2008) 211-213.

[461] Langtry S, *Corporate Governance,* (2005) 3-5.

[462] Cunningham G M & Harris J E, Enron and Arthur Andersen: The Case of the Crooked E and the Fallen A, (2006) *Global Perspectives on Accounting Education,* Vol. 3(1), 27-48.

المنارة للاستشارات
www.manaraa.com

Undoubtedly, Enron was voted as having one of the best boards in America before its collapse and was recognized for its commitment to corporate governance practices.[463] It therefore, follows that investors and other stakeholders must recognise that although laws and regulations might be essential they are not sufficient in compelling directors to act in a manner that achieves good corporate governance.[464] As long as directors have no respect for law as individuals, no enforcement mechanisms will prevent abuse of power and thus corporate collapses.

It has thus been convincingly argued that self-regulation, in which an organisation voluntarily monitors its own adherence to legal and ethical standards, provides for more flexibility and adaptability than having government agents monitoring and enforcing those standards.[465] This approach allows organisations to maintain control over the standards to which they are held by effectively self-policing themselves. The risk with strict regulation is that directors may focus so much on conformance and neglect their principal task, namely profit making of the company.[466] Apart from the bureaucratic burden that would be imposed by external enforcement, the cost of setting up such a mechanism is also avoided.[467] Moreover, even if clear rules are followed, one can still find a way to circumvent their underlying purpose which is harder to achieve if one is bound by a broader principle. The continued corporate failures as a result of abuse of power and remuneration by directors is thus an indication that South Africa still has a lot of work towards grooming competent and honesty directors who are able to self-police themselves as well as to improve its quality of enforcement mechanisms.

---

[463] Ibid.

[464] Trebeck K, Exploring the Responsiveness of Companies: Corporate Social Responsibility to Stakeholders, (2008) *Social Responsibility Journal*, Vol 4(3) 349-365.

[465] Bosch H, The changing face of Corporate Governance, (2002) *University of New South Wales Law Journal*, Vol 25(2) 270-293.

[466] Ibid.

[467] Corporations in South Africa fail to strictly adhere to statutorily stated formalities because adherence to these can be very time consuming and financially costly. (See Cooper M. S, *Corporate Governance In Developing Countries: Shortcomings, Challenges & Impact on Credit,* (2007) 3-5).

المنارة للاستشارات
www.manaraa.com

3.2.2 Insufficient Board Independence and Balance of Power

With respect to director responsibility, the inquiries following recent corporate scandals and failures have revealed that the board of directors was often not sufficiently independent from management, and as a result, did not inquire thoroughly about questionable practices proposed and undertaken by executive management.[468] In particular, it has been noted that there is a shortage of truly independent non-executive directors in South Africa and that ownership and control are highly concentrated in individual companies or groups of companies.[469] As a result of the skills shortage, some South African companies have continued to have the same person in the role of both chairman and chief executive officer, been unable to constitute audit and remuneration board committees comprising of sufficient independent non-executive directors and have found it difficult to maintain properly balanced boards.[470] This tends to compromise the system because if corporate governance is to mean more than conformance, then the board should be composed in such a way that it reflects the necessary skills, experience and expertise for the organisation being governed.[471] Furthermore, the checks and balances on directors' powers and remuneration meant to be achieved, by for instance *King Code* recommendations, are compromised and not as effective as they would otherwise have been.

---

[468] Van Melle Kamp C, Corporate Governance in Africa – the Impact on Non-executive Directors, (2005) *Professional Management Review*, Vol 16 (9) 14.

[469] Wixley T. & Everingham G, *Corporate Governance,* (2005) 22-24. The authors argue in relation to the King recommendation regarding nonexecutive directors, that in South Africa there is a relatively small pool of persons possessing the requisite business acumen and experience who are available to act as non-executive directors.

[470] According to the Deutsche Bank Securities Incorporated Corporate Governance Survey of 2002, only 1% of South African companies had no independent directors on their board. However, 58% of the companies had not yet met the requirement to have a majority of board members independent. A total of 42% of the companies in the survey had independent directors representing at least half of the board of directors. Two companies, of the 73 companies analysed, Gold Fields Ltd Metals & Mining and SAB Plc Beverages, tied for greatest board independence. It can thus be concluded that the overwhelming prevalence of independent directors illustrates the adoption of certain elements of the *King Code* and relative maturity of the corporate structure in South Africa (Deutsche Bank Securities Incorporated, *Global Corporate Governance*, *Valuing Corporate Governance in South Africa*, (2002) 13-14).

[471] Mcgregor L, *Improving Corporate Governance in South Africa,* Discussion paper submitted for the 1st USB Colloquium on Corporate Governance, 18th September 2008, available at http://www.governance.usb.ac.za/downloads/UnitColloquiumPaper1_LynnMcGregor.pdf. (visited on 12 January 2010).

www.manaraa.com

Another observation has been that some non-executive directors in South Africa have treated their directorships as "honorary appointments rather than positions imposing fiduciary duties and accountability to the company and its shareholders, and therefore to be undertaken only with due care and diligence."[472] It therefore follows that, South Africa's policy makers and regulators have not done enough towards stimulating Boards of Directors to take independent decisions as fiduciaries of corporations and not to just implement controlling shareholders' decisions without applying their minds and questioning the rationale behind the decisions.

On a positive note, the current increased focus on the negligence by directors of their duties may have a beneficial impact in the long term as current and future directors become aware of the real duties that accompany a board appointment and the risks of failing to comply. Although some companies have not managed to separate the duties of chairman and chief executive officer, it is also worth noting that other companies are increasing the number of non-executive directors on their boards as well as splitting the roles of chairman of the board and CEO in an effort to enhance corporate governance, for instance AngloGold Ashanti Limited.[473]

However, another challenge that may continue to haunt South Africa is that as a result of higher levels of compliance required from boards, individuals are less likely to risk financial harm or to compromise their reputations by serving on boards.[474] Given the new liabilities imposed on directors in the Companies Act, it may also be difficult for companies to find people willing to act as directors since they can be sued in their personal capacity for almost any loss that is suffered due to a company's actions. The responsibilities of non-executive directors and additional time commitment required are also increasing to a point where there is now greater reluctance from competent

---

[472] Ibid.

[473] Deutsche Bank Securities Inc, Global Corporate Governance, *Valuing Corporate Governance in South Africa*, (2002) 12-13.

[474] Langtry S, *Corporate Governance,* (2005) 13.

المنارة للاستشارات
www.manaraa.com

personnel to take on the role of non-executive directorship in the companies.[475] Furthermore, as companies begin to restrict outside board service for executive directors, the pool of talented independent directors may shrink and there might be an upward pressure on salaries required to attract competent and committed candidates.[476]

It can therefore, be concluded that although South African boards have tried to balance their composition, the directors have found ways of going around the measures in place to satisfy their personal needs at the expense of the company. The balancing of power and independence within the board, though necessary to achieve good corporate governance, has not been sufficient to completely deter directors from abusing their powers and earning unjustified remuneration. It is, however, important to appreciate that if this corporate governance principle was non-existent and completely not observed even more corporate failures as a result of power abuse and excessive remuneration would have occurred.

3.2.3 Shareholder Passivity

Research has revealed that, despite the frequency of poor or undesirable corporate governance practices by company directors which should be of concern to shareholders, South Africa has faced challenges in that many institutional investors do not participate in shareholders' meetings and company business.[477] This mentality needs to be changed because investors have fiduciary duties and need to fulfil them by voting and demanding more from companies where they put their trust and their investments. Shareholder participation should assist as a checking mechanism on the way directors exercise their powers and remunerate themselves and ensures that chances of mismanagement are reduced or detected early enough. It has also been argued that participation by various

---

[475] PricewaterhouseCoopers (PwC), *Non-executive Directors: Increased Responsibility and a Shrinking Pool of Talent,* (Johannesburg 2008) 2-3.

[476] Ibid.

[477] Vaughn *et al*, Corporate Governance in South Africa: A Bellwether for the Continent? (2006) 504-512.

المنارة للاستشارات
www.manaraa.com

stakeholders may complement other internal and external monitoring mechanisms and thereby promote greater managerial accountability and compliance.[478]

However, the other challenge in achieving meaningful shareholder participation has been that some companies in South Africa do not disclose sufficient information to equip the shareholders to enable them to make objective judgments on the governance practices of the companies in which they invest.[479] Some directors have, for example, not sufficiently disclosed their remuneration in the financial statements as well the business areas where they might not have observed good corporate governance. As a result of lack of adequate information, shareholders have been incapacitated to make informed decisions and to influence the behaviour of the directors when they are not content with their conduct. What this has therefore meant for South Africa is that, despite the existence of the legal and regulatory framework aimed at empowering shareholders, the prevailing environment has been such that it does not motivate shareholders to effectively participate in their companies' business.

3.2.4 Corruption

Another contributing factor to the continued incidences of poor corporate governance practices is the high rate of corruption in South Africa. To show the high level of corruption in South Africa, the Transparency International 2009 Corruption Perceptions Index gave South Africa a score 4.7 out of 10, placing it 55th out of 180 countries surveyed.[480] The country's low ranking in the global corruption perception index may pose a threat to lasting corporate governance improvement in the country as it may hinder the effective implementation and enforcement of laws and regulations. Research

---

[478] The Department of Trade and Industry and King's College London, *Key Drivers of Good Corporate governance and the Appropriateness of UK Policy Responses* (2007), available at http://www.berr.gov.uk/files/file36671.pdf (visited on 26 May 2009).

[479] Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, (2008) 211-213.

[480] The Transparency International 2009 Corruption Perceptions Index (CPI) available at http://www.guardian.co.uk/news/datablog/2009/nov/17/corruption-index-transparency-international.

المنارة للاستشارات
www.manaraa.com

has shown that corruption and ineffective government bureaucracies are the most important constraints on economic growth, followed by lack of finance.[481] The effect of corruption is that corporate governance-related laws and regulations may not be enforced (or may be enforced selectively) and the reliability of the judicial system may be compromised. This leaves shareholders and other stakeholders with little or no recourse to deal with their complaints, for example where they witness directors abusing their powers and getting excessive remuneration.[482] Another challenge is that in South Africa, like in many countries, too much focus is placed on those who demand or accept bribes and not enough is done to individuals and business companies who offer inducements to commit corruption.[483] South Africa therefore, has to work towards addressing corruption if it is to realize its full gains for the efforts put towards obtaining a corporate governance system that effectively limits directors' powers and regulates their remuneration.

3.2.5 Insufficient Disclosure or Reporting

South Africa has sufficient laws and regulations relating to information disclosure and reporting[484] which has resulted in the majority of companies making sufficient disclosures to its investors and other stakeholders. An important observation from the survey by Deutsche Bank Securities Incorporated was that there was increased disclosure by companies of the remuneration of the board of directors. The survey indicated that 47% of South African companies had an independent compensation committee and that two-thirds of South African company directors receive a significant part of their remuneration in company equity "which is positive and in line with international standards of best practice, as it aligns the interest of directors and minority

---

[481] Stuart Cohn, Teaching in a Developing Country: Mistakes Made and Lessons Learned in Uganda, 48 J. *Leg. Educ*. (1998), 101- 104.

[482] Deutsche Bank Securities Inc, Global Corporate Governance, *Valuing Corporate Governance in South Africa*, (2002) 32.

[483] Langtry S, *Corporate Governance,* (2005) 4.

[484] See discussions on *King Report* (paragraph. 2.2.6.2.2.), the Companies Act (paragraph 2.2.6.3.3) and *JSE Listing Requirements* (paragraph 2.2.6.4) above.

المنارة للاستشارات
www.manaraa.com

investors."[485] Also positive was the fact that 67% of boards had defined performance criteria by which to evaluate the performance of directors. In addition the survey revealed that that about two-thirds of South African companies had adequate information disclosure with some companies having gone beyond the minimum requirements of the country's laws and regulation in their disclosure of information.[486]

Although there are sufficient laws and regulations relating to information disclosure and reporting the culture of disclosure regarding South African corporations, generally, is yet to match international standards.[487] The main challenge is that some companies and directors view disclosure as a liability and unnecessary cost to the company and thus do not accord it the preference it deserves. Additionally, companies argue that revealing sensitive information to the public decreases their competitive edge since their competitors can obtain more information on the inner workings of the company.[488] As a result companies are hesitant to make full disclosure such that where the information is disclosed in financial statements and annual reports it is sometimes inadequate to enable sound decision making by shareholders and other stakeholders.[489] Research has shown that, in South Africa, nondisclosure of information is still widespread on selection of external auditors, whistle blowing and other directors' benefits, among others.[490]

Despite these shortcomings, disclosure and accountability as key elements of good corporate governance are increasingly embraced by South African corporations,

---

[485] Deutsche Bank Securities Inc, Global Corporate Governance, *Valuing Corporate Governance in South Africa*, (2002) 13-15.

[486] Although the requirement in South Africa is for semi-annual disclosure, the Anglogold, BHP, Billiton Plc, Harmony, Avgold Ltd, Gold Fields Limited, Sappi, among others, disclose quarterly results. (Deutsche Bank Securities Inc, Global Corporate Governance, *Valuing Corporate Governance in South Africa*, (2002) 13-14).

[487] Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, (2008) 49-52.

[488] Clinch G & Verrechia R E, Competitive Disadvantage and Discretionary Disclosure in Industries. (1997) *Australian Journal of Management*, 22 (2) 125-138.

[489] Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, (2008) 211-213.

[490] Ibid.

المنارة للاستشارات
www.manaraa.com

particularly those who compete at the international level.[491] It can therefore, be concluded that, although there are laws and regulations aimed at enhancing transparency and accountability through disclosure, there is still room for improvement in so far as directors' powers and remuneration are concerned.

3.3 Conclusion

From the above, it can be acknowledged that policy makers and regulators in South Africa have put a lot of effort in promoting good corporate governance so as to align the country with global standards. The legal and regulatory reforms have played a significant role in enhancing corporate governance in South Africa at the same time acting as effective restraints on directors' powers and remuneration.[492] There, however, remain a number of challenges the country has to attend to in order to achieve full compliance with corporate governance principles. The main challenges that South Africa has encountered are, among others, lack of competent and committed human resources; poor regulatory oversight; lack of adherence to the regulatory framework, and inadequate transparency and disclosure; inadequate legal and judicial frameworks; corruption and ineffective compliance mechanisms.[493] Furthermore, many of the regulatory bodies that are meant "to provide checks and balances within the system (including prosecuting systems)" have insufficient resources, skills, infrastructure, and independence to enforce the laws and regulations.[494]

---

[491] For example, some companies, such as Anglo American, Dimension Data, and Liberty, started to publish individual director remuneration well before such disclosure was required. (Deutsche Bank Securities Incorporated, Global Corporate Governance, *Valuing Corporate Governance in South Africa*, (2002) 14).

[492] From the discussions above, it may be concluded that, the fact that the principles of corporate governance are usually contained in existing legal rules and statutes (for instance the Companies Act which deals with the duties of a company director), peer pressure, shareholder activism and the role of the media as a "watchdog" has, to a certain extent, motivated directors to comply with corporate governance principles.

[493] Cooper M. S, *Corporate Governance In Developing Countries: Shortcomings, Challenges & Impact on Credit,* (2007) 3.

[494] Ibid.

المنارة للاستشارات
www.manaraa.com

The above analysis indicates that, although South Africa has tried to put in place stringent legal and regulatory measures to restrain directors from abusing their powers or engaging in any form of misconduct, these have not been sufficient to achieve 100% good corporate governance compliance. The failure of stringent requirements to achieve full corporate governance compliance shows that there is more to corporate governance than just laws and regulations; directors have to be committed to practice good corporate governance.[495] While regulatory systems and enforcement schemes may encourage directors to follow the law, ultimately the decision to act responsibly must come from within the individuals as no law or regulations are adequate to guide directors' behavior. As such directors who belief in corporate governance regard compliance with regulations as a minimum standard for performance, go far beyond merely meeting the requirements on a checklist and do not need laws like the Sarbanes-Oxley to conduct themselves professionally, ethically and honestly. Judging from the efforts already put by policy makers, the concerns about abuse of power, excessive remuneration and corporate collapses can therefore, be a thing of the past if directors choose to practice good corporate governance.

South African legislatures and policy makers therefore, still have a lot of work towards enhancing voluntary compliance, strengthening enforcement and prosecution mechanisms, encouraging sufficient disclosure and reporting, reducing corruption and encouraging shareholders' participation so as to successfully restrain directors' powers and regulate their remuneration thus achieve good corporate governance.

[495] Vaughn *et al*, *Corporate Governance in South Africa: A Bellwether for the Continent?* (2006) 504-512.

المنارة للاستشارات
www.manaraa.com

CHAPTER 4

COMPARISON BETWEEN SOUTH AFRICAN AND UNITED KINGDOM CORPORATE GOVERNANCE LAWS AND REGULATIONS

4.1 Introduction

A number of lessons can be derived by developing and emerging economies in the way corporate governance has been practiced in developed economies.[496] Corporate governance law is reformed to keep abreast of developments in the world and the changing business environment. It is thus critically important that whenever a country decides to put enabling legislation in place it is compatible with international best practice.

However, as the King Committee observed, companies are governed within the framework of the laws and regulations of the country in which they operate.[497] In view of the fact that countries differ in culture, regulation, law and generally the way business is conducted, there can be no single generally applicable corporate governance model. Despite the need for countries to have laws and regulations that match their individual circumstances, there are certain international standards[498] that every country is required to comply with taking into consideration the fact that investors now invest internationally. In this regard, four pillars have been considered essential to all international guidelines of corporate governance namely fairness, accountability,

---

[496] Leong Ho Khai, *Reforming Corporate Governance in Southeast Asia: Economics, Politics and Regulations,* (ISEAS Publications 2005) 38 available at www3.ntu.edu.sg/.../HoKhaiLeong/Ho%20Khai%20Leong%20vita%20October%202007.pdf.

[497] Introduction and Background to the *King II Report*.

[498] International guidelines have been developed by, among others, the Organisation for Economic Cooperation and Development (OECD), the International Corporate Governance Network (ICGN), and the Commonwealth Association for Corporate Governance (CACG) to guide member and nonmember countries.

المنارة للاستشارات
www.manaraa.com

responsibility and transparency.[499] The principles are intended to assist OECD and non-OECD governments when they decide to review and develop the legal, institutional and regulatory framework for corporate governance in their countries to match their individual developmental experiences.[500] The principles also provide guidance and suggestions for regulatory bodies like stock exchanges and for investors, corporations, directors and other parties that have a role in the process of developing good corporate governance. As indicated above, the principles are to be used only as guidelines which means governments, public or private sectors should continue to develop more detailed "best practice" in corporate governance applicable to their specific situations.[501]

It is therefore, desirable that South Africa should harmonise with other jurisdictions to reduce the cost and increase certainty both for international companies and investors, and for the benefit of local companies involved in international trade and investment. To establish the extent to which South Africa has tried to harmonise its systems with other international players, a comparison of its corporate governance reforms is made to reforms that have been done in the United Kingdom. Noteworthy is the fact that this comparative analysis is based on specific corporate governance aspects (directors' powers and remuneration) which have been considered relevant to the research. It is therefore, not the purpose of this study to set out and analyse comprehensively all the corporate governance principles and guidelines in South Africa and United Kingdom.

In view of the importance of duties of directors in corporate governance, the research first makes a comparison of the duties of directors as provided in United Kingdom and South African company law and then focuses on other corporate governance initiatives aimed at curbing abuse of directors' powers and payment of excessive remuneration.

---

[499] OECD Principles of Corporate Governance, (OECD, April 1999).

[500] Tumuheki J, *Towards Good Corporate Governance: An Analysis of Corporate Governance Reforms in Uganda,* (2008) 29-30.

[501] Ibid.

المنارة للاستشارات
www.manaraa.com

4.2 Company Law - Duties of Directors

South Africa company law is heavily influenced by the United Kingdom system such that its Companies Act 61 of 1973 is based on a framework and general principles derived from English law.[502] In both South Africa and the United Kingdom, directors are subjected to various duties which include statutory[503] and common law duties.[504] Directors must act in good faith, with due care and diligence and in the best interests of the company. Historically, directors' duties in both South Africa and the United Kingdom were owed almost exclusively to the company and its members but more recently there has been a move towards recognition of a wide range of other stakeholders' interests which include employees, creditors and the community, among others. The United Kingdom Companies Act has plainly revealed that it favours the enlightened shareholder value approach[505] as indicated by the specific listing of different stakeholders' interests in section 172 of the Companies Act.[506] On the other hand, South Africa has not categorically indicated its preferred option and contains elements of both shareholder primacy and stakeholder protection.[507] Although not clearly stated, in South Africa "in the interests of the company" has been interpreted to mean that directors are

---

[502] Naidoo R, *Essentials for Corporate Governance for South African Companies, (*2002) 10-12.

[503] Examples of statutory duties are found in sections 234–240 of the current Companies Act 61 of 1973 and section 75 and 76 of the new Companies Act 71 of 2008 of South Africa and sections 171-177 of UK Companies Act 2006 which provides for general duties of directors. In terms of both countries' Companies Acts directors are subjected to penalties for violating their statutory duties.

[504] See chapter 2 paragraph 2.1 for a full discussion on the South African directors' duties.

[505] In the "enlightened shareholder" approach the legitimate interests and expectations of stakeholders only have an instrumental value and stakeholders are only considered in as far as it would be in the interests of shareholders to do so.

[506] Esser I & Du Plessis J J, The Stakeholder Debate and Directors' Fiduciary Duties, (2007), 19 *South African Mercantile Law Journal* 346-363. Section 172 of the UK Companies Act, Cap. 46 of 2006 explicitly states that it is the directors' duty to promote the success of the company for the benefit of its members as a whole, and in fulfilling this duty the directors must have regard to both short and long term factors and wider interests including employees, trade partners, the community and the environment (enlightened shareholder value approach).

[507] Esser I & Du Plessis J J, The Stakeholder Debate and Directors' Fiduciary Duties, (2007) 346-363. It has been argued that, although South Africa's New Companies Act does not contain provisions analogous to section 172 of the UK Companies Act 2006, section 7 of the South African New Companies Act, read together with section 76 of the New same Act, appears to indicate that directors are required to consider the company's impacts on non-shareholders, which includes, *inter alia*, ensuring compliance with the Bill of Rights in the application of company law.

المنارة للاستشارات
www.manaraa.com

expected to recognise the importance of other stakeholders over and above the company itself.[508]

Another development in the two countries' company law is that duties of directors have been codified in terms of the Companies Acts.[509] The United Kingdom has codified the common law fiduciary duties of directors as well as the duty of care, skill and diligence. In terms of paragraph 305 of the explanatory notes[510] to the Companies Act[511] the statement of directors' duties is intended to be exhaustive although it has been argued that the new codification does not present a full codification of the existing law.[512] The main reasons advanced for the codification as recommended by the Company Law Review (CLR) include the need to provide greater clarity on what is expected of directors and make the law more accessible and predictable.[513]

The United Kingdom Companies Act codifies the duty to act within power,[514] duty to promote the success of the company,[515] duty to exercise independent judgment,[516] duty to exercise reasonable care, skill and diligence,[517] duty to avoid conflict of interest,[518]

---

[508] In support of this Mervyn King says: *"Directors in the twenty-first century have to be seen to be directing companies to be good corporate citizens. The inclusive approach recognizes that a company is a link that brings together the various stakeholders relevant to the business of the company".* (King M, *Governance for all Entities*, 2006.) The *King III Code* recommends a "stakeholder inclusive" approach of governance (*Introduction and Background- Inclusive stakeholder approach*).

[509] See paragraph 2.2.3.2 for a discussion on codification of directors' duties in South Africa.

[510] The United Kingdom Explanatory Notes to the Companies Act, 45, available at the Department of Trade and Industry website at http://www.dti.gov.uk. (visited on 25 August 2009).

[511] United Kingdom Companies Act, Cap.46 of 2006.

[512] Esser I, *Recognition of Various Stakeholder Interests in Company Management*, (2008) 290-292.

[513] The United Kingdom Explanatory Notes to the Companies Act, 45-47. Commentators have argued that, although the codification of directors' duties brings about more certainty it does not necessarily guarantee sufficient flexibility.

[514] Section 171 of the UK Companies Act, Cap. 46 of 2006.

[515] Ibid s 172.

[516] Ibid s 173.

[517] Ibid s 174.

[518] Ibid s 175.

المنارة للاستشارات
www.manaraa.com

duty not to accept benefits from third parties,[519] and duty to declare interest in proposed transaction or arrangement.[520] Section 171(4) provides that "the general duties shall be interpreted and applied in the same way as common law rules or equitable principles, and regard shall be had to the corresponding common law rules and equitable principles in interpreting and applying the general duties." This means that the wealth of jurisprudence available in decided cases is not lost and is to be referred to in interpreting the codified duties. It is also acknowledged that codified duties do not cover all the duties that a director may owe to the company as many other duties are imposed else-where in legislation, such as the duty to file accounts and reports with the registrar of companies.[521]

For almost the same reasons the United Kingdom codified its directors' duties, South Africa also partially codified its directors' duties with section 76 of its Companies Act 71 of 2008 providing for standards of directors conduct.[522] The section states that a director, when acting in that capacity or as a member of a committee of directors, is subject to a duty to exercise the degree of care, skill and diligence and a fiduciary duty to act honestly and in good faith, and in a manner the director reasonably believes to be in the best interests of, and for the benefit of, the company. The section further provides that in addition to the general duty of care, and fiduciary duty, a director must comply with the Act and the company's memorandum of incorporation, and communicate to the board any material information that comes to his attention. Section 76(6) provides that the provisions of the section are in addition to, and not in substitution for, any duties of the director of a company under the common law. This means that, like in the case of United Kingdom, regard will be had to common law duties of directors in aspects not covered under the Act. Similarly, many of the South African directors' duties are imposed else-where in legislation for example in the Income Tax Act and National Environmental Management Act.

---

[519] Ibid s 176.

[520] Ibid s 177.

[521] The United Kingdom Explanatory Notes to the Companies Act, 45-48

[522] See paragraph 2.2.3.2 for a discussion on codification of directors' duties in South Africa.

المنارة للاستشارات
www.manaraa.com

What is clear from the above is that, both South African Companies Act 71 of 2008 and United Kingdom Companies Act of 2006 acknowledge that despite the attempted codification, some of the directors' duties remain uncodified. In both cases reference is made to the continued applicability of common law duties. However, the Companies Act of United Kingdom provides a more detailed statutory standard for directors' duties than the South African Companies Act. In both countries, directors' conduct play an important role in ensuring that their companies conform to good corporate governance practices hence the efforts to make the duties easily accessible, clearer and predictable.

4.3 Recent Developments in Corporate Governance

Any chronological review of corporate governance systems in the United Kingdom tends to start with the 1992 report of the Cadbury Committee on the financial aspects of corporate governance which was mainly a result of several corporate scandals[523] and excessive remuneration plans in the late 1980's.[524] When the United Kingdom business community became worried with the huge remuneration packages for some directors, referred to in the British press then as "fat cat" directors, it recognised a clear need to improve the strength of its governance.[525] This led to the establishment, in 1991, of the Committee on the Financial Aspects of Corporate Governance, chaired by Sir Adrian Cadbury, which issued a series of recommendations known as the *Cadbury Report* in 1992.

---

[523] Examples of corporate collapses include the Bank of Credit and Commerce International, Polly Peck International, and the Robert Maxwell pension fund.

[524] Maassen G F, *An international Comparison of Corporate Governance Models*, 3rd Edition (Gregory Maassen 2002) 124-126.

[525] Ferri F& Maber D, *Say on Pay Vote and CEO Compensation: Evidence from the UK*, (Harvard Business School 2008), available at http://69.175.2.130/~finman/Reno/Papers/FMASayOnPay.pdf (visited on 15 February 2010).

المنارة للاستشارات
www.manaraa.com

The *Cadbury Report* addressed a number of issues of corporate governance that were not dealt with in existing company law.[526] To ensure compliance with the *Cadbury Report,* a requirement was introduced within the Listing Rules of the London Stock Exchange that companies should report whether they had followed Cadbury's recommendations, or explain why they had not done so (the so-called "comply or explain" principle). The recommendations in the *Cadbury Report* have been reviewed and refined at regular intervals since 1992.

In 1995 the *Greenbury Report* set out recommendations on the remuneration of directors.[527] In 1998 the *Cadbury* and *Greenbury Reports* were brought together and updated in the form of the *Combined Code*. In 1999 the *Turnbull* guidance was issued to provide directors with guidance on how to develop an effective system of internal control. As a result of the Enron and WorldCom scandals in the US, the *Combined Code* was updated (in 2003) to incorporate recommendations from reports on the role of non-executive directors (the *Higgs Report*) and the role of the audit committee (the *Smith Report*).[528] In the same year, the United Kingdom Government appointed the Financial Reporting Council (FRC) to assume responsibility for publishing and maintaining the Code.[529]

[526] According to Maassen, "the Committee placed much stress on the need for strong and independent non-executive directors in corporate boards to avoid the repetition of corporate affairs like Maxwell". The *Cadbury Report* also stressed the need to split the positions of the CEO and chairman to achieve a clear division of power in the top of corporations. The formation of standing oversight board committee, for example the audit committee, was also encouraged to support boards' control roles. In addition to these recommendations, the *Cadbury Report* recommended corporations to reconsider the remuneration schemes and bonus plans for executive directors and to reconsider the position of the independent auditor (Maassen G F, *An international Comparison of Corporate Governance Models*, (2002) 127).

[527] The key themes in the *Greenbury Report* were accountability, responsibility, full disclosure, alignment of director and shareholder interests and improved company performance. Due to public and shareholder concerns about excessive remuneration packages, the *Report* emphasized the need of corporations to publicly disclose more information on the remuneration of directors. The *Code* contains detailed provisions that supplement the requirements of the Companies Act on the disclosure of board remuneration elements in annual financial reports. Another requirement for listed corporations, introduced by Greenbury, was to set up a remuneration committee consisting exclusively of non-executive directors ". . . with no personal financial interest other than as shareholders in the matters to be decided, no potential conflicts of interest arising from cross-directorships and no day-to-day involvement in running the business" (Paragraph 14 of the *Greenbury Report*).

[528] Financial Reporting Council, *The United Kingdom approach to Corporate Governance*, (2006) available at http://www.frc.org.uk/documents/pagemanager/frc/FRC%20The%20UK%20Approach%20to%20Corporate%20Governance%20final.pdf (visited on 10 November 2009).

[529] Ibid.

المنارة للاستشارات
www.manaraa.com

Contrary to the position in the United Kingdom, in South Africa corporate governance was not motivated by any considerable crisis in the corporate sector at that time; "rather it concerned the competitiveness of the South African private sector following the re-admission of the country to the global economy following its transition to a fully-fledged democracy after the collapse of apartheid."[530] The *King Code*, released in November 1994, was the product of a committee convened by the Institute of Directors following the publication of the *Cadbury Report* in United Kingdom. The committee extensively based its corporate governance framework on the United Kingdom model[531] and used the *Cadbury Report* as a guide for its work, using the same structure for its report but at the same time considered special circumstances prevailing in South Africa that necessitated a deviation from this approach.[532] The main aim of the *Report* was to encourage the highest standard of corporate governance in South Africa by recommending standards of conduct for directors and emphasizing the need for responsible corporate conduct

Later, the adoption of a new Constitution, economic developments locally and internationally as well as corporate scandals such as Macmed, Regal Treasury Bank and LeisureNet necessitated the revision of the *King Report*, and the second *King Report* was published in 2002. In September 2009, the King Committee on Corporate Governance released the *King III Code* of Governance Principles and the *King III Report on Governance for South Africa*. This was necessitated by the anticipated new Companies

---

530 Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 9.

531 The corporate governance issues in South Africa are thus heavily influenced by twentieth century United Kingdom jurisprudence mainly due to the fact that because of its colonial history its company law is based on the United Kingdom (English) system. (Sarra, J. P, *Strengthening Domestic Corporate Activity in Global Capital Markets: A Canadian Perspective on South Africa's Corporate Governance,* 2004).

532 Malherbe S and Segal N, *Corporate Governance in South Africa*, 2001, 49-51. For example, whilst the report agreed with Cadbury that the splitting of the roles of chief executive and chairman was "undoubtedly correct in principle", it went on to say that: "There are, however, many circumstances in South Africa where the positions of chair and chief executive are combined in the same individual, due to force of circumstances. There are, for example, "family companies" in South Africa, many of which are listed on the Johannesburg Stock Exchange".

المنارة للاستشارات
www.manaraa.com

Act and changes in international corporate governance trends since the release of the *King II* in 2002.[533]

From the above, one can conclude that South Africa has lagged behind the United Kingdom in so far as the number of codes of corporate governance is concerned. However, it is also important to note that, although South Africa has lagged behind it is not the number of codes that matters but the comprehensiveness. In this regard South Africa has tried to capture the majority of the issues captured in the United Kingdom's different corporate governance codes into the *King Code* which makes the *Code* more comprehensive, easier to understand and more user-friendly.

4.4 Application of Corporate Governance Codes

In its preamble, the United Kingdom *Combined Code* states that the Code applies to listed companies and encourages small listed companies to adopt the approach in the Code where provisions are relevant in their case. The Code's principles and recommendations were incorporated into the *Listing Rules* of the London Stock Exchange and are mandatory for listed companies for reporting years commencing on or after 1 November 2003.[534] The *London Stock Exchange Listing Rules* require corporations to provide a statement of compliance with the principles and guidelines of the *Combined Code* in two parts. The first requires corporations to indicate how the principles of the Code are applied and the second requires corporations to provide an explanation when they do not comply with certain provisions of the Code.[535] Companies

---

[533] The Institute of Directors in Southern Africa and the King Committee on Governance, *King III Report on Corporate Governance for South Africa*, 2009. Events at Fidentia also happened at an appropriate time for South Africa to be able to identify some weaknesses in its corporate governance system (Keynote Address by Tshediso Matona, Director-General: Trade and Industry, *Conference on South African Company Law for the 21st Century*, Pretoria, 19 March 2007).

[534] Institute of Chartered Accountants in England and Wales, *Corporate Governance Developments in the UK*, available at http://www.icaew.com/index.cfm/route/149243/icaew_ga/en/Technical_and_Business_Topics/Topics/Corporate_governance/Corporate_governance_developments_in_the_UK (visited on 27 January 2010).

[535] Ibid.

المنارة للاستشارات
www.manaraa.com

listed on Alternative Investment Market (AIM)[536] in the United Kingdom are not formally required to comply with the *Combined Code* but some choose to do so.

In a slightly different approach from the *Combined Code*, the *King III* applies to all entities regardless of their nature, size or form of incorporation or establishment.[537] The Code further provides that it should be applied in addition to requirements contained in statutes, regulations and other authoritative directives regulating the conduct and operation of such enterprise.[538] Similar to the United Kingdom's situation, the *King III Report* principles and recommendations were incorporated into the *JSE Listings Requirements* and are mandatory to listed companies. Some of the provisions of the *King Code of Corporate Governance* are compulsory for companies listed on the JSE which must report compliance with the Code in their annual statements. Each company director must certify that he or she is satisfied that the company has complied with the *Listing Requirements*. The *JSE Listing Requirements* provides that applicant issuers must include in the pre-listing statement, a narrative statement of how it has applied the principles set out in the *King Code*, a statement of the company's compliance with the Code and the reasons for each and every instance of non-compliance.[539]

The *Combined Code* is not prescriptive, it works on a "comply or explain" basis; which means companies may choose not to comply with specific provisions but, in that case, will have to provide a proper public explanation of their decision. In a slightly different approach the South African *King III* moves from a "comply or explain" approach[540] to a

[536] The Alternative Investment Market (AIM) is a sub-market of the London Stock Exchange, allowing smaller companies to float shares with a more flexible regulatory system than is applicable to the main market. AIM's regulatory model is based on a comply-or-explain option that lets companies that are floated on AIM either comply with AIMs relatively few rules, or explain why it has decided not to comply with them.

[537] The *King II Report* applied to all companies with securities listed on the JSE securities exchange, banks, financial and insurance entities, and public sector enterprises and agencies that fall under the Public Finance Management Act. Nevertheless, the *King II Report* also encouraged other companies not mentioned to give due consideration to the application of the code insofar as the principles are applicable.

[538] Introduction and Background to the *King III*.

[539] Section 7 of *JSE Listing Requirements*.

[540] The *King I* and *II Codes* applied a "comply or explain" approach.

المنارة للاستشارات
www.manaraa.com

principles-based "apply or explain" approach where entities are expected by way of explanation to make a positive statement about how the corporate governance principles have been applied or have not been applied. There are indications that it is likely that the *Combined Code* will follow this trend in its future updates.[541]

Over and above the Codes on Corporate governance, the regulation of corporate governance in the United Kingdom is enhanced through, inter alia, common law rules (e.g. directors' fiduciary duties); statute (notably the Companies Act), a company's constitutional documents (the Memorandum and Articles of Association) and the *Listing Rules*. In a similar manner, regulation of corporate governance in South Africa is further improved through, among others, Acts of Parliament, particularly the Companies Act, common law and the *JSE Listings Requirements*.

Having discussed the general similarities and difference between South Africa and United Kingdom corporate governance mechanisms, what follows are discussions on specific provisions of the Codes that relate to directors' powers and remuneration. The main idea behind discussing the various provisions is to analyse and compare the provisions as well as assess their effectiveness in restraining directors' powers and regulating remuneration in both countries.

4.4.1 Composition of the Board

The *King Codes* recommend that there should be a balance of power and sufficient independence within the board to prevent the dominance of the board by one individual or by a small number of individuals. In this regard the Code recommends that the board should have a majority of non-executive directors and a sufficient number of non-executive directors should be independent of management.[542] They also recommend that

[541] *SA Unveils King III*, Issued on Behalf of The Institute of Directors By PR Republic, available at http://www.link2media.co.za/index.php?option=com_content&task=view&id=5412&Itemid=12 (visited on 17 February 2010).

[542] See paragraph 2.2.2.3 for a discussion on this aspect in relation to South Africa. See also chapter 2 of the *King II* and *King III Codes*.

المنارة للاستشارات
www.manaraa.com

at least one third of the non-executive directors should rotate every year and that the board should include a statement in the integrated report regarding the assessment of the independence of the independent non-executive directors.[543] They further recommend that audit, nominating and remuneration committees should be composed of independent non-executive directors.

Likewise, the United Kingdom *Combined Code* provides that there should be an effective board, with an appropriate balance of executive and non-executive directors and in particular independent non-executive directors such that no individual or small group of individuals can dominate the board's decision making.[544] The *Code* further provides that "except for smaller companies, at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent".[545] Both the *Combined Code* and the *King Code* recommend that there be transparency in the appointment of directors preferably through a nomination committee and that performance evaluation be conducted for the board and each individual director.[546] Due to the fact that most corporate collapses were as a result of lack of truly independent directors,[547] both the United Kingdom *Combined Code* and the South African *King III Code* provide for re-evaluation of directors' status as "independent non-executives" after nine years.[548] The main idea behind both *Codes* recommending involvement of independent directors at a large scale is to ensure that there is a suitable balance of power and that there is objective and unbiased review of the actions of executive directors and management in meeting agreed goals and objectives.

---

[543] Ibid.

[544] Section 1 of the *Combined Code*.

[545] Section 1 of the *Combined Code*.

[546] Individual evaluation should aim to show whether each director continues to contribute effectively and to demonstrate commitment to the role (including commitment of time for board and committee meetings and any other duties).

[547] In failed companies such as Regal Bank and Leisurenet in South Africa and Polly Peck International and Robert Maxwell in United Kingdom, part of the problem that led to their downfall was a lack of truly independent directors (Maassen G F, *An international Comparison of Corporate Governance Models*, (2002) 127-128).

[548] Chapter 2 of the *King III Code* and section 1 of the *Combined Code*.

المنارة للاستشارات
www.manaraa.com

4.4.2 Separation of Chief Executive Officer (CEO) and Chairman's roles

Both the *King Code* and *Combined Code* state that there should be a clear division of responsibilities at the helm of the company in that the Chief Executive Officer (CEO) of the company should not also fulfil the role of chairman of the board.[549] The Codes further state that where the roles of the chairperson and chief executive are combined, there should be either an independent non-executive director serving as deputy chairperson, or a strong independent non-executive director element on the board.[550] Additionally, where these roles are combined, this needs to be justified each year in the company's annual report.[551] In a slightly different approach, the *Combined Code* provides that if under exceptional circumstances a board decides that a chief executive should become chairman; the board should consult major shareholders in advance and should set out its reasons to shareholders at the time of the appointment and in the next annual report.[552] The *King III* just provides that the appointment of a chairman, who is not independent, should be justified in the integrated report and the CEO should not become the chairman until 3 years have lapsed.[553] All these conditions are set to ensure that there is sufficient separation of duties and powers of the Chairman and the CEO and to avoid abuse of authority if one becomes too powerful.

4.4.3 Role and function of the board

The *King* and *Combined Codes* recommend that the board and its directors should act as the focal point for and custodian of corporate governance and in the best interests of the

[549] Ibid. See also paragraph 2.2.2.5 for a discussion on this aspect in relation to South Africa.

[550] Ibid.

[551] Ibid.

[552] Section 1of the *Combined Code*.

[553] Chapter 2 of the *King III Code*.

المنارة للاستشارات
www.manaraa.com

company.[554] Directors therefore, have to know what is expected of them in so far as performing their duties is concerned so that they exercise their duties within the confines of their powers. To ensure that directors are adequately guided, the *King III* recommends that every board should draft a charter setting out its responsibilities which should be disclosed in the annual report and consider developing a code of conduct dealing with conflicts of interest. Similarly, the *Combined Code* recommends that a company's annual report should include a statement of how the board operates, including a high level statement of which types of decisions are to be taken by the board.

4.4.4 Shareholders Participation

It is generally believed that shareholders have a key role to play in driving long-term company performance and economic prosperity as well as promoting good corporate governance.[555] The United Kingdom Companies Act broadly provides for shareholder participation in the governance of companies through enhancing the power of proxies and enfranchising indirect investors. Such provisions include: access to timely and transparent company information,[556] exercising rights through proxy,[557] facilitating ecommunication,[558] shareholders' right to sue directors for negligence (derivative claims),[559] and the right to petition against unfair prejudice.[560] Furthermore, the *Combined Code* outlines a number of guiding principles for shareholder activism that go beyond voting at annual general meetings and legal actions against directors. These

---

[554] Chapter 2 of the *King III Code* and Section 1 of the *Combined Code*. See also paragraph 2.2.2.2 for a detailed discussion on this aspect in relation to South Africa.

[555] The UK Companies Act, 2006, Regulatory Impact Assessment, January 2007. Available at http://www.dti.gov.uk/files/file29937.pdf. (visited on 26 August 2009). See also paragraph 2.2.2.8 for a discussion on this aspect in relation to South Africa. See also paragraph 2.2.2.8 for a detailed discussion on this aspect in relation to South Africa.

[556] Ibid ss 146-151, 423-432.

[557] Ibid ss 324-331.

[558] Ibid s 147(4), Parts 3 & 4 of Schedule.

[559] Ibid s 260.

[560] Ibid s 994.

المنارة للاستشارات
www.manaraa.com

principles are meant to encourage continuous engagement of shareholders in company business so that they provide a checking mechanism on directors' conduct.[561]

On the other hand, in South Africa, four basic rights of shareholders are identified: a right to capital, a right to income, a right to vote and a right to information.[562] As a result in the explanatory memorandum,[563] it is stated that "the law should protect shareholder rights, advance shareholder activism and provide enhanced protection for minority shareholders". The Companies Act 71 of 2008 provides for shareholder meetings, facilitation of proxy voting and electronic voting, shareholders' right to information, application to protect shareholders' rights, application to declare a director delinquent or under probation, application for relief from oppression or prejudicial conduct, dissenting shareholders' appraisal rights, and derivative actions.[564] Similar to *Combined Code,* the *King Reports* have also made a number of recommendations to encourage corporate-governance-focused shareholder activism, for example, educating shareholders in corporate governance, review of quorum requirements to encourage participation at general meetings and establishment of shareholder watch-dog organizations to look after the interests of minority shareholders.[565]

Both the *King Report* and the United Kingdom *Combined Code* therefore, seek to create an environment for shareholders to be more than speculators, to be owners concerned with the well-being of the company in which they invested, and constantly to check whether the directors of the company practice good corporate governance.[566]

---

[561] Tumuheki J**,** *Towards Good Corporate Governance: An Analysis of Corporate Governance Reforms in Uganda,* (2008) 48-50.

[562] Department of Trade and Industry (DTI) *Policy Document* (Note 62) 37.

[563] Explanatory Memorandum to the South Africa Companies Bill, 2007, 5.

[564] Sections 26, 31, 39, 41, 58-65 and 161-165 of Companies Act 71 of 2008.

[565] Institute of Directors in Southern Africa, *Executive Summary of the King Report 2002*, (IOD 2002). See also Introduction and Background and Chapter 8 of the *King III*.

[566] Rademeyer C and Holtzhausen J, King II, Corporate Governance and Shareholder Activism, (2003) *SALJ,* Vol 120 (4) 767.

المنارة للاستشارات
www.manaraa.com

4.4.5 Remuneration of Directors

The *King III* recommends that directors should be remunerated fairly and responsibly and that the remuneration policies should be aligned with the strategy of the company and linked to individual performance.[567] It further recommends that companies should disclose the remuneration of each individual director and certain senior executives.[568] In addition to the *King Code*, the South African Companies Acts,[569] and the *JSE Listing Requirements*[570] provide for disclosure of directors remuneration in the company's financial statements and annual reports. Disclosure assists in achieving transparency and enables shareholders and other interested stakeholders to evaluate the reasonableness of the directors' remuneration.

Whilst South Africa's *King III* addresses the issue of directors' remuneration, the United Kingdom has had more instruments to deal with this aspect. For example on realising that the original Cadbury recommendations did not adequately cover the issue of executive remuneration, the United Kingdom came up with the *Greenbury Report* which resulted in the *London Stock Exchange Listing Rules* being expanded to incorporate, amongst other things, remuneration committees, remuneration policy and share options and other long term incentive schemes relating to each director.[571] Further to the *Greenbury Report,* the United Kingdom also came up with the "Directors' Remuneration Report Regulations 2002"[572] which require the directors of a company to prepare a

---

[567] See paragraph 2.2.6 for a discussion on this aspect in relation to South Africa. Also see Chapter 2 of the *King III Code*.

[568] Ibid.

[569] See sections 295-297 of the Act 61 of 1973 which require directors to disclose loans to directors, security for benefit of directors, directors' emoluments, pensions paid and the amount of any compensation paid to directors and past directors in respect of loss of office. Similarly, section 30 of Act 71 of 2008 requires directors to disclose, in the company's financial statements, the remuneration and benefits received by each director as well as details of any other payment made.

[570] See sections 7 and 8 of the *JSE Listing Requirements*, available at http://www.jse.co.za/ listing_requirements.jsp.

[571] Point S and Tyson S, Top Pay Transparency in Europe: Codes, Convergence and Clichés, (2006) *The International Journal of Human Resources Management*, Vol 17 (5) 812-830.

[572] The Directors' Remuneration Report Regulations 2002 at http://www.hmso.gov.uk/si/si2002/20021986.htm.

المنارة للاستشارات
www.manaraa.com

remuneration report that is clear, transparent and understandable to shareholders. The regulations require that the remuneration report gives details of, among others, company's policy on directors' remuneration and amounts paid to each director as emoluments and compensation in the relevant financial year.[573] The main objective of the Regulations, as stated by the Department of Trade and Industry (DTI) are to enhance transparency in setting directors' pay, improve accountability to shareholders and to provide for a more effective performance linkage.[574]

Like the *King Codes*, the *Combined Code* provides that remuneration should not be excessive when considered against prevailing market norms and that some element should be performance related.[575] The remuneration policy should be clear and no director should be involved in determining his or her own remuneration.[576] There should also be full disclosure in the annual report and accounts.[577] However, the revised *Combined Code* does not include detailed material in the previous Code on the disclosure of directors' remuneration because the Directors' Remuneration Report Regulations 2002 are now in force and supersede the earlier Code provisions. In a similar manner to South Africa, the United Kingdom Companies Act[578] and the *London Stock Exchange Listing Rules* provide for disclosure of directors remuneration as a way of enhancing transparency.

To ensure that there is enhanced transparency and that the remuneration paid to directors is subjected to some form of scrutiny and does not go unchecked, both countries' governance codes provide for establishment of remuneration committees. The *Greenbury Report* provides for the setting up of remuneration committees of non-

---

[573] See schedule 7A of The Directors' Remuneration Report Regulations 2002.

[574] Deloitte, *Report on the impact of Directors' Remuneration Report Regulations*, A Report for the Department of Trade and Industry, available at www.berr.gov.uk/files/file13425.pdf (visited on 13 June 2009).

[575] See section 1 of the *Combined Code*.

[576] Ibid.

[577] See schedule C of the *Combined Code.*

[578] See section 412-413 and 420-422 of UK Companies Act, 46 of 2006.

المنارة للاستشارات
www.manaraa.com

executive directors to determine within agreed terms of reference the company's policy on executive remuneration and specific remuneration packages for each of the executive directors, including pension rights and any compensation payments.[579] The *Report* further recommends that remuneration committees must provide the packages needed to attract, retain and motivate directors of the quality required but should avoid paying more than is necessary for this purpose.[580]

The remuneration committee should make a report each year to the shareholders on behalf of the Board which should form part of, or be annexed to, the company's Annual Report and Accounts.[581] The report should also include full details of all elements in the remuneration package of each individual director by name, such as basic salary, benefits in kind, annual bonuses and long-term incentive schemes including share options.[582]

Similarly, the *King Codes* recommend the setting up of a remuneration committee (comprised of independent non-executive directors or chaired by such) which should assist the board in setting and administering remuneration policies that address all forms of payments to directors.[583] The committee should come up with a remuneration policy which should be aligned with the strategy of the company, linked to individual performance and aim to attract and retain quality directors.[584] Shareholders should pass a non-binding advisory vote on the company's yearly remuneration policy and the board should determine the remuneration of executive directors in accordance with the remuneration policy put to shareholder's vote.[585] The *King Codes* also recommend that the company's annual report should also include full details of all elements in the

---

[579] See paragraphs 4.3-4.7 of the *Greenbury Report*.

[580] See paragraphs 6.5-64.7 of the *Greenbury Report*.

[581] The report should be the main vehicle through which the company accounts to shareholders for directors' remuneration. See paragraph 5.4 of the *Greenbury Report*.

[582] See paragraphs 5.8-5.12 of the *Greenbury Report*.

[583] Chapter 2 of the *King III Code*.

[584] Section 1 of the *King II* and chapter 2 of the *King III*.

[585] Chapter 2 of the *King III Code*. See also section 1 of the *Combined Code* for a similar provision.

المنارة للاستشارات
www.manaraa.com

remuneration package of each individual director. All these recommendations positively restrict payments of excessive remuneration to directors.

4.5 Enforcement of compliance

Both countries have come up with a number of legal and regulatory provisions as a way of ensuring that directors conduct their duties within the confines of their powers and comply with formalities and legal requirements. In addition to imposing criminal liability in conjunction with civil liability, the South African Companies Act contains a wide range of purely criminal provisions.[586] In most instances directors are liable in addition to the company for contraventions by the company[587] although in some cases one's liability is based entirely on his own conduct.[588] Over and above this, the Companies Act provides for remedies in respect of common law[589] for example, subsection (2) of section 77[590] provides that the section applies in addition to any rule of common law that is consistent with the section. This means that the provisions of the common law can also be applied to a director or company for misconduct or any breach of the provisions of the Act.

Like the South African Companies Act, section 178 of the United Kingdom Companies Act provides for the continuation of existing civil remedies for breach or threatened breach of general duties. If a director breaches the provisions of sections 171 to 177 (general directors' duties) the corresponding common law rule or equitable principle is

[586] Section 216 of the Companies Act 71 of 2008 provides that any director who is convicted of any offence referred to in the Act is liable to a fine and can be sentenced to a maximum period of ten years depending on the nature of the offence. See also Mammatt J, Du Plessis D & Everingham G, *The Company Director's Handbook*, (Cape Town:Siber Ink 2004) 100-12 for a list of all the criminal offences in the Companies Act.

[587] Many of the contraventions by the company involve non-compliance with formalities.

[588] See, for example, s 216(5) of the Companies Act, which makes it a criminal offence for a director to fail to notify the company of a change in personal particulars.

[589] In support of this view, section 158 of Act 71 of 2008 provides that "when determining a matter brought before it in terms of this Act, or making an order contemplated in this Act *a* court must develop the common law as necessary to improve the realization and enjoyment of rights established by this Act".

[590] Section 77 of the South Africa Companies Act 71 of 2008 provides for liability of directors.

المنارة للاستشارات
www.manaraa.com

applied.[591] At common law, directors can be held liable either because of their own independent conduct, or as joint wrongdoers, or as criminal associates.[592] The Explanatory Notes to the United Kingdom Companies Act state that in the case of fiduciary duties, the consequences of breach may include damages or compensation where the company has suffered loss, restoration of the company's property, an account of profits made by the director; and rescission of a contract where the director failed to disclose an interest.[593] The above is in addition to other remedies available to the shareholders of the company.

In a further effort to deter would be fraudulent directors from not complying with requirements, the South African Companies Act[594] provides for the disqualification of directors and for a register of disqualified directors to be maintained by the registrar of companies. It also provides for the removal of directors by way of an ordinary resolution before the expiration of his period of office.[595] Similarly, the United Kingdom Companies Act provides that a company may, by ordinary resolution, "remove a director before the expiration of his period of office, notwithstanding anything in any agreement between it and him".[596] With regards to the disqualification of directors, the United Kingdom had to promulgate a separate Act[597] to deal with the matter. On the other hand, in United Kingdom a director who contravenes the provisions of the Companies Act can

---

[591] Section 178 of UK companies Act, Cap.46 of 2006.

[592] Kathleen Van Der Linde, The Personal Liability of Directors for Corporate Fault–An Exploration, (2008) 439-442.

[593] The United Kingdom Explanatory Notes to the Companies Act at 45, available at the Department of Trade and Industry website at http://www.dti.gov.uk. South Africa has case law and statutory provisions which provide for similar penalties in addition to other remedies available to the shareholders of the company.

[594] Section 162 of Companies Act 71 of 2008. See also section 69 which prohibits a person who has been disqualified from acting as director and a disqualified person under this section includes a person who has been declared by court to be a delinquent director or placed under probation in terms of section 162.

[595] Section 220 of the Companies Act 61 of 1973 and section 71 of the Companies Act 71 of 2008. See also *Swerdlow v Cohen* 1977 (1) SA 178 (W) at 182E-G.

[596] Section 168 of UK Companies Act, Cap 49 0f 2006.

[597] Company Directors Disqualification Act 1986 (c.46). The Act sets out the procedures for company directors to be disqualified in certain cases namely general disqualification for misconduct (ss 2-5), disqualification for unfitness (ss 6-9) and other cases of disqualification (ss 10-12). A person who contravenes a disqualification order is guilty of an offence and can be imprisoned for a period of up to 12 years (s 13) and is furthermore personally liable for the company's debts (s 15).

المنارة للاستشارات
www.manaraa.com

be subjected to harsh penalties not exceeding the statutory maximum on the standard scale.[598] All these provisions are aimed at ensuring that directors perform their duties and exercise their powers within the confines of the relevant legal and regulatory provisions in both countries.

Furthermore, to enforce compliance, both countries have regulatory bodies tasked to ensure that companies and their directors comply with corporate governance requirements as well as other laws and regulations.[599] As indicated above, the JSE and the London Stock Exchange have also played a significant role in ensuring that all companies listed with the two are obliged to comply with certain corporate governance principles as enshrined in the *King Code* and *Combined Code* respectively.

Despite the above similarities, the two countries have some differences. The United Kingdom approach, for example, combines high standards of corporate governance with relatively low associated costs. Studies consistently show that the United Kingdom outperforms South Africa and other countries with comparable standards in terms of governance standards and compliance costs.[600] For this reason, the United Kingdom model is increasingly used as a template for corporate governance reform in other countries for example in the European Union, where 26 out of 27 Member States have adopted United Kingdom-style corporate governance codes during the last few years.[601]

---

[598] Examples are sections 165 and 167 of the UK Companies Act 2006 which provide that a person guilty of an offence under sections "is liable on summary conviction to a fine not exceeding level 5 on the standard scale and, for continued contravention, a daily default fine not exceeding one-tenth of level 5 on the standard scale".

[599] Examples of the regulatory bodies in United Kingdom are the Financial Reporting Council (FRC), Financial Services Authority (FSA) and the Financial Reporting Review Panel (the FRRP). Similarly South Africa has the Financial Services Board (FSB), the South African Reserve Bank, the Securities Regulation Panel and the Public Accountants and Auditors Board as examples of its regulatory bodies.

[600] Financial Reporting Council, The *UK Approach to Corporate Governance,* November 2006, available at www.frc.org.uk/.../FRC%20The%20UK%20Approach%20to%20Corporate%20Governance%.pdf (visited on 26 August 2009).

[601] UK Institute of Directors, *The UK Model of Corporate Governance: An Assessment from the Midst of a Financial Crisis*, available at http://www.iod.com/intershoproot/eCS/Store/en/pdfs/policy_publication_The_UK_Model_of_Corporate_Governance.pdf (visited on 12 March 2010).

المنارة للاستشارات
www.manaraa.com

Another area of difference is that South Africa seems to be increasingly placing confidence in the "power of rules to keep companies on the straight and narrow" especially if one looks at certain provisions of the Banks Amendment Act and the Companies Act 71 of 2008 which contains more than twenty sections that deal with directors' liability, ranging from how to punish false statements in a company prospectus to stipulating ways to protect shareholders' rights.[602] The approach in the United Kingdom, on the other hand, appreciates the view that a risk-free society is basically not possible and thus continues to place greater reliance on principles and outcome-focused rules as a way to achieve regulatory aims, and less reliance on prescriptive rules.[603] Much of the United Kingdom's success is attributed to the conservative approach its regulators have taken by leaving the promotion of good corporate practices to the business sector.[604] The regulators chose to be involved in promoting good governance through appointment of committees or groups comprising predominantly of private sector which has proved to be very effective.[605]

Additionally, the United Kingdom, being a developed country, has better enforcement mechanisms as it is better financially resourced than South Africa. This makes its legal and regulatory mechanisms more effective as it has adequate resources, both human and capital, to equip its judicial system. In contrast, South Africa's enforcement mechanism is characterized by insufficient resources and lengthy delays in the judicial process.[606] Another advantage that United Kingdom has over South Africa is that it has low levels of corruption[607] which makes enforcement of corporate governance principles easier.

---

[602] Horn R. C, *Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 58-59. However, the country's *King III* still strongly recommends that compliance with corporate governance principles remains voluntary to allow for flexibility (Introduction and Background to *King III Report on Corporate Governance*).

[603] Maimonis A, *Rule-Focus Ed Approach Makes Corporate Governance a Snag,* Businessday, 17 September 2009, 2.

[604] Horn R. C, *Legal Regulation of Corporate Governance with Reference to International Trends*, (2005) 41-42.

[605] Ibid.

[606] Armstrong *et al*, Corporate Governance: South Africa, a Pioneer in Africa, (2005) 24-28.

[607] The Transparency International 2009 Corruption Perceptions Index (CPI) gave United Kingdom a score of 7.7 out of 10, placing it 17th out of 180 countries and South Africa a score of 4.7 out of 10, placing it 55th out of 180 countries surveyed. Available at http://www.guardian.co.uk/news/datablog/2009/nov/17/corruption-index-transparency-international (visited on 17 February 2010).

المنارة للاستشارات
www.manaraa.com

Corruption hinders the effective implementation and enforcement of laws and regulations hence the reason why South Africa lags behind the United Kingdom in implementing and enforcing corporate governance. Last but not least, research has shown that a large percentage of the South African population lags far behind the United Kingdom as far as knowledge, skills and experience to run, manage and direct companies are concerned.[608] This means that the United Kingdom is better placed to have board of directors that are properly balanced, have appropriate skills and sufficient independence to enable effective practice of good corporate governance.

4.6 Conclusion

South Africa and the United Kingdom have a lot in common in terms of their corporate governance frameworks which closely resemble one another. This is mostly because of South Africa's colonial history which has resulted in its corporate governance being based on the United Kingdom model in a common law framework. The corporate governance Codes of both countries (*King* and *Combined*) make almost similar recommendations as a way of restricting directors from abusing their powers and being paid excessive salaries. These range from advocating for a balance of powers on the board, separation of roles of chairman and chief executive officer, encouraging shareholder participation to setting up of remuneration committees, disclosure of directors' remuneration and imposing stiff penalties for defaulting directors. Another area of similarity is that the two countries have amended their company legislation to codify directors' duties[609] a move that is being internationally recognised and that is aimed at clarifying and making the duties easily accessible and predictable. Furthermore, both the JSE Securities Exchange and the London Stock Exchange make it a listing requirement for all listed companies to apply certain corporate governance principles as a way of promoting corporate governance.

---

[608] Du Plessis J J, *A Comparative Analysis of Directors' Duty of Care, Skill and Diligence in South Africa and in Australia,* Paper presented at the 2009 Corporate Law Teachers Association, hosted by the UTS, Sydney in February 2009, available at www.clta.edu.au/professional/papers/conference2009/du_PlessisCLTA09.pdf (visited on 15 February 2010).

[609] The only difference is that South Africa has partially codified the duties whilst the United Kingdom has fully codified the duties.

المنارة للاستشارات
www.manaraa.com

The analysis in paragraph 4.5 above has also revealed that the level of compliance with corporate governance by companies and directors is greater in the United Kingdom than in South Africa mostly because the United Kingdom is more developed than South Africa, has a larger pool of directors who qualify as independent directors and it started implementing corporate governance principles earlier. Another major distinguishing development in the United Kingdom company law was the drafting of the Directors' Remuneration Report Regulations which have been in force since 2002 and the *Higgs* and *Greenbury Reports* which all give general guidelines on directors' remuneration.

Although South Africa appears to be favouring more prescriptive rules and regulations, it continues to strive to promote self-regulation in corporate governance as evidenced by the provisions of its new *King III Code*. The United Kingdom framework on the other hand, has sought to achieve a favourable balance between "hard law" (for example the Companies Act, the Financial Services Authority (FSA) Listing Rules) and "soft law" (best practice principles as stipulated in the *Combined Code* as an example). Nevertheless, it appears that a key aspect of both countries' approach is that many of the principles of best practice are not defined by company law, but arise from the corporate governance codes. This reflects the view that not all aspects of corporate governance behaviour should (or can) be defined by the inflexible requirements of formal legislation. Despite the different levels of enforcement and compliance, on the whole both countries have made significant and commendable efforts to promote good corporate governance especially in so far as restraining the directors' powers and regulating their remuneration.

المنارة للاستشارات
www.manaraa.com

CHAPTER 5

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The essential role of corporate governance has certainly been recognised in South Africa as evidenced by the spectrum of instruments that have been put in place to improve governance. The country maintains a reasonably good legal and institutional infrastructure for corporate governance, with such features as a comprehensive set of corporate governance-related laws and regulations and the existence of regulatory agencies and private sector bodies committed to improving corporate governance.

However, what is clear from the research is that there are still gaps in the country's legislative and regulatory frameworks and considerable weaknesses in its quality of enforcement especially in so far as restricting directors' powers and regulating their remuneration is concerned.[610] Although most companies observe good corporate governance, a number of companies, institutions and state-owned enterprises still fall short of practising real good corporate governance as shown by allegations of questionable business practices that continue to capture the newspaper headlines. It therefore, follows that, although much has been achieved there is still more to be done to encourage directors and everybody else to uphold the principles of corporate governance so that the country fully realises the benefits of good corporate governance.

[610] Chapter 3 paragraph 3.2.1.

المنارة للاستشارات
www.manaraa.com

5.2 Summary of Findings

The research sought to establish the legal and regulatory mechanisms South African policy-makers and committees have put in place to promote good corporate governance and to assess the effectiveness of these mechanisms with particular emphasis on directors' powers and remuneration.

In chapter 1, the motivation behind carrying out the research was explained,[611] the term corporate governance was defined[612] and its importance explained.[613] Although many definitions were discussed, corporate governance was summarised to mean, systems by which companies are directed and controlled with major emphasis being placed on transparency, independence, fairness and accountability. It was highlighted that good corporate governance assists in the attraction of investment on favourable terms both locally and internationally, enhances company performance and improves the management of the company or country, among others.

In chapter 2, the duties and powers of directors and the legal and regulatory framework on directors' powers and remuneration were discussed. The discussion on directors' duties and powers was basically done to bring out the nature of conduct expected from directors which, if properly observed, should assist in achieving good corporate governance. Company directors are subject to various duties which include statutory and common law duties.[614] Common law duties are categorised into fiduciary duties of good faith and the duty to act with the necessary care and skill when performing the duties.[615] The research also established that, over and above the profit maximisation objective,

---

[611] Chapter 1 paragraphs 1.1 & 1.2.

[612] Chapter 1 paragraph 1.3.

[613] Chapter 1 paragraph 1.4.

[614] Chapter 2 paragraphs 2.2.1 .1.2 & 2.2.1.1.3. An example of a statutory duty is the duty to disclose conflict of interest that a director may have in a contract in terms of section 75 of the Companies Act 71 of 2008.

[615] Chapter 2 paragraphs 2.1.2 and 2.2.3.

المنارة للاستشارات
www.manaraa.com

directors are now expected to recognise a wider variety of interests than only those of shareholders when acting "in the interests of the company".[616]

After the general discussion on directors' duties, the *King Report on Corporate Governance*, the Companies Act and the *JSE Listing Requirements* were discussed as the main legal and regulatory sources of corporate governance in South Africa.[617] It was established that South Africa has made substantial strides in coming up with a number of legal and regulatory measures to guard against abuse of power and payment of excessive remuneration by company directors.[618] Important to note amongst the corporate governance initiatives are the recommendations of the *King Reports*, the statutory provisions of the Companies Act and the listing conditions of the JSE. The first significant move was the introduction of the *King Report on Corporate Governance* (*King I*) whose recommendations made an important contribution to the remarkable progress South Africa has made towards corporate governance reform. The *King I* was reviewed to come up with the *King II Report* which has also been reviewed and updated in line with international best practices resulting in the *King III Report* which was implemented in March 2010.

South Africa has also reviewed its Companies Act 61 of 1973 to align it with international best practices and promulgated a new Companies Act (Act 71 of 2008) in 2009.[619] Similarly, the *JSE Listing Requirements* have been continuously updated in line with global trends. To add to this, a series of statutory interventions and regulations have also been introduced or substantially revised which have had a direct impact on corporate governance and a restrictive effect on directors' powers and remuneration.[620] Furthermore, South Africa has established a number of regulatory bodies and offices to

[616] Chapter 2 paragraph 2.1.1.

[617] Chapter 2 paragraphs 2.2.2, 2.2.3 & 2.2.5

[618] Chapter 2 paragraph 2.2.

[619] Chapter 2 paragraph 2.2.3.1.

[620] Chapter 2 paragraph 2.2.

المنارة للاستشارات
www.manaraa.com

improve the quality of enforcement and encourage compliance.[621] All this has been done with the realisation and acknowledgement of the importance of upholding good corporate governance practice both at company and national level.

The *King Reports* recommended that there be a balance of power within boards, clear specification of directors' responsibilities, separation of roles of chairman and chief executive officer, effective participation of shareholders, setting up of remuneration committees and disclosure of directors' remuneration, among others.[622] All these recommendations, if appropriately applied, are aimed at ensuring that directors' conduct does not go unchecked, there is a balance of power and sufficient independence within the board and that directors' remuneration is linked to company performance. On the other hand, the Companies Act 71 of 2008 has codified directors' duties to ensure that the directors are clear about their obligations and the associated liabilities or remedies in case of violation of those duties.[623] A number of regulatory provisions ranging from statutory duties of directors, compulsory disclosure of directors' remuneration, the requirement of shareholder approvals before certain things are done, personal liability for wrongful acts and stiff penalties have also been set in the Companies Act as a way of enforcing compliance by directors.[624]

Likewise, the *JSE Listing Requirements* are such that they provide a checking and balancing mechanism on the directors' powers and excessive remuneration. The *Listing Requirements* require companies to, among others, observe certain provisions of the *King Report*, separate the position of chairman and chief executive and disclose directors' remuneration and other information.[625] In addition, the *Listing Requirements*

[621] Chapter 2 paragraph 2.2.7.4.

[622] Chapter 2 paragraphs 2.2.2.2 to 2.2.2.8.

[623] Chapter 2 paragraph 2.2.3.2.

[624] Chapter 2 paragraphs 2.2.7.2.

[625] Chapter 2 paragraph 2.2.7.3.

المنارة للاستشارات
www.manaraa.com

may impose stiff penalties on defaulters and publicise their names and details of offences.[626]

In chapter 3, an evaluation of the effectiveness of the legal and regulatory mechanisms put in place as discussed in chapter 2 was done. The research revealed that South Africa's corporate governance has significantly improved and most companies, particularly listed companies consider corporate governance sincerely.[627] It was also established that the legal and regulatory mechanisms, although not sufficient, have significantly manage to restrict directors' powers and remuneration. The main concern, however, is that there is no full compliance with the *King Report on Corporate Governance* mostly due to poor enforcement and prosecution[628] as well as the fact that South African companies and directors tend to comply with the requirements but not with the spirit of good corporate governance.[629] There has also been insufficient board independence and balance of power in the companies due to skills shortage.[630] The skills shortage has also resulted in the checking mechanisms on directors' powers and remuneration being compromised and not being as effective as they would have been were the boards composed of people with the necessary skills, experience and expertise.[631]

Further to the above, although there are a number of statutory and regulatory provisions empowering shareholders to participate in company business and act as a checking mechanism, the shareholders have been passive and not effectively taken interest in monitoring the performance of the companies in which they have invested in.[632] This has

---

[626] Ibid.

[627] See chapter 3, paragraph 3.1.

[628] Chapter 3 paragraph 3.2.1.

[629] Ibid. This was also confirmed by the research done by KPMG in 2006 which indicated that many JSE listed companies develop the *King 11* checklists and tick off compliance without necessary buying into the spirit of good governance (KPMG, Survey of Integrated Sustainability Reporting in South Africa, (2006) 19-23).

[630] Chapter 3 paragraph 3.2.2.

[631] Ibid.

[632] Chapter 3 paragraph 3.2.3.

المنارة للاستشارات
www.manaraa.com

tended to compromise their role as a checking and advisory tool on directors' conduct. Corruption has also adversely affected the effectiveness of the legal and regulatory measures in that corporate governance-related laws and regulations have not been fully enforced and the reliability of the judicial system has been compromised.[633] In addition, the disclosure and reporting culture in South African companies is yet to match international standards. Companies, for instance, fail to provide adequate inside information about company practices in annual reports to enable sound decision making by shareholders and other stakeholders.[634] It therefore, seems like a lot of effort needs to be put to develop the necessary human capital and systems that will continue to strengthen the good framework that is in place thus putting the various codes of good practice into action.

In chapter 4, the South African corporate governance legal and regulatory mechanisms were compared and contrasted with those of the United Kingdom with a view to assess South Africa's standing internationally. The comparative analysis with the United Kingdom revealed that South Africa has kept up to date with international developments and the changing business environment and competes favourably with some developed countries.[635] The analysis also confirmed that the two countries have a lot in common[636] generally preferring voluntary compliance with corporate governance principles to compulsory enforcement by statutory and regulatory agents.

With regards to directors' powers and remuneration the United Kingdom's legal and regulatory framework has provided almost similar restraints and regulations to those of South Africa. As a way of limiting directors' powers and remuneration, the United Kingdom *Combined Code* recommends, among others, that the board be properly

---

[633] Chapter 3 paragraph 3.2.4.

[634] Chapter 3 paragraph 3.2.5.

[635] Chapter 4 paragraph 4.6.

[636] Ibid. Examples being codification of directors' duties, similarities between Codes of Corporate Governance and the enforcement of the Codes through Stock Exchange Authorities.

المنارة للاستشارات
www.manaraa.com

composed with sufficient independent directors, the chairman be separated from the chief executive officer, shareholders be encouraged to participate in company business and that there be a remuneration committee to come up with remuneration policies. Like South Africa, the United Kingdom's Companies Act and *Listing Rules* have provided for various penalties to deter directors from beaching their fiduciary duties and practising bad corporate governance.[637] To complement the legal and regulatory instruments, the United Kingdom has also established various regulatory bodies to ensure that directors exercise their powers and are remunerated within the confines of the relevant laws and regulations.[638] However, the United Kingdom has also not yet achieved 100% good corporate governance especially with regards to limiting directors' powers and regulating their remuneration.

5.3 Conclusions

The research has revealed that corporate governance has become an increasingly important issue in South Africa which will, for the foreseeable future, continue occupying an important place in greater debates on what legal and regulatory frameworks ought to look like in order to promote sustainable good corporate governance practice. The legislatures and committees should be complimented for the *King Code on Corporate Governance*, Companies Act, *JSE Listing Requirements* and other measures which have significantly strengthened the corporate governance framework in that together they form a comprehensive framework for ensuring that private and public companies are effectively managed. The country's efforts have, to a certain extent, successfully managed to limit directors' powers and regulate their remuneration despite the occurrence of incidences of corporate collapses resulting from dominance by individuals or a small group of people.

[637] Chapter 4 paragraph 4.5

[638] Ibid.

المنارة للاستشارات
www.manaraa.com

However, given the efforts that South Africa has put to improve its corporate governance standards, what is apparent from the number of corporate collapses that continue to occur is that the most effective internal monitors of corporate governance are the directors and no law or regulations are adequate to guide directors' behavior. As a result, legislative measures for corporate governance are considered by some commentators to be unnecessary on the grounds that rules are often broken and the forcible imposition of rules is unlikely to be effective unless directors voluntarily observe business ethics.[639] It therefore, follows that overly prescriptive approaches like Sarbanes-Oxley and some of the legislation currently being considered in South Africa might not solve the corporate governance challenges as there are limits to legislating on corporate governance since a lot depends on the integrity and ethical values of the directors. Policymakers, investors and other stakeholders must therefore, recognise that although the law is necessary, it is not a sufficient factor in compelling directors to act in a manner that achieves good corporate governance as even the most stringent corporate governance standards may be inadequate to curb multifaceted fraud and other corrupt tendencies.[640] Moreover, even if clear rules are followed, one can still find a way to circumvent their underlying purpose, a situation which is harder to achieve if one is bound by a broader principle.

It can thus be persuasively argued that, self-regulation in which an organisation voluntarily monitors its own observance of legal and ethical standards, is a better option than to have an outside agency such as government monitoring and enforcing those standards. The advantage with policing oneself is that the company and directors are able to maintain control over the standards to which they are held without being pushed by external forces.[641] An additional advantage is that the company and directors are able

[639] Langtry S, *Corporate Governance*, (2005) 13. As an example, the requirement for disclosure of material balance sheet transactions should in theory prevent undisclosed corporate loans to directors but rules can be circumvented and some other way of channeling money to individuals could well be found that is not in breach of the law but would not require disclosure.

[640] See Chapter 3 paragraph 3.2.1.

[641] Other commentators however, believe that self-regulation which relies on monitoring without enforcement by either exchanges or governments, or where there is limited or no outside monitoring, is unlikely to yield fruitful results. (DeJong A, DeJong D. V, Mertensa G, Wasley C, The Role of Self-Regulation in Corporate Governance: Evidence and Implications from The Netherlands , (2005) *Journal of Corporate Finance*, 11, 473–503).

المنارة للاستشارات
www.manaraa.com

to avoid the cost of setting up a mechanism to the specification of the outside agency. Making governance codes part of the law should thus be avoided as it eliminates the adaptability and flexibility originally intended.

Although self-regulation would be desirable, the continued corporate governance failures points to the fact that there are some aspects of directors' duties that require certain legislative and regulatory controls.[642] One can therefore, be persuaded to conclude that market led enforcement, along with strengthening of company law mechanisms constitutes the best equilibrium for developing adaptive but nevertheless effective corporate governance practices. Companies and directors should thus be left to voluntarily practice good corporate governance by implementing various corporate governance principles that are relevant to their business.[643] However, with respect to specific items, if it appears that the corporate governance code provisions have not been effective, and that the directors and business community refuse to abide by it, the law should step in. For that reason, there is need for a balance and a combined effort between statutory and self-regulatory measures on directors' powers and remuneration to motivate directors to adhere to good corporate governance practices. A partially regulated structure has the effect of minimizing costs but at the same time encouraging compliance.

5.4 Recommendations

In light of the summary and conclusions above, there is need to strike a balance between legislative and regulatory measures to restrain directors from abusing the powers vested in them and to effectively regulate their remuneration. The main recommendations arising from this research study are discussed below.

[642] Such regulation should, however, not suppress the companies' ability to attract and retain directors, nor should it discourage robust yet responsible entrepreneurship and risk-taking.

[643] To be effective good governance needs to be implemented in a way that fits the culture and organisation of the individual company. This can vary enormously from company to company depending on factors such as size, ownership structure and the complexity of the business model. (See paragraph 4.1 above).

المنارة للاستشارات
www.manaraa.com

5.4.1 Induction and training of directors

From the above analysis, it would appear that it is the quality and morality of the individual directors that play an instrumental role in ensuring good corporate governance practices. Despite the important role directors play, there seems to be a general lack of adequate attention to the induction and training of directors in both private and public institutions. What might be important therefore, is to professionally develop individuals that are engaged as directors through comprehensive formal induction and training so that they become competent to act as such. Sufficient resources should therefore be channeled towards training facilities and programs for corporate directors and developing strong audit committees of Boards of Directors. To further assist the process, there should be sufficient disclosure of the qualifications and biographical information of all directors to help in identifying training needs and to assure shareholders and other stakeholders that the members can effectively fulfil their responsibilities. There should also be disclosure of the mechanisms which are in place to act as "checks and balances" on the competence of key individuals in the enterprise.

The training required would differ depending on whether one is an executive or a non-executive director. In the case of non-executive directors, the training process might include learning about the company's business, what is expected of them as directors, professional ethics and getting to know its key executives. On the other hand, training of executives could also involve learning about the statutory and regulatory duties, responsibilities, professional ethics and potential liabilities of directors. The bottom line message is that, without a satisfactory level of knowledge and competence in these areas, directors in general and non-executive directors in particular will be unable to satisfactorily perform their duties and comply with formalities. Directors should therefore, be encouraged to continually update their skills and the knowledge and familiarity with the company required to fulfil their roles so that they are able to effectively discharge their duties. This would also ensure that the country has a reasonable pool of appropriately qualified and independent directors especially in cases

المنارة للاستشارات
www.manaraa.com

where directors are required to have specialist knowledge such as those who serve on the audit committee of a board.

It is important to note that the training of directors should not present implementation challenges as the costs involved can always be minimised by conducting in-house training as well slotting in relevant topics at directors' groupings without necessarily holding formal training sessions. The only minor challenge might be the need to convince the directors of the necessity for training and the importance of leaving their busy schedules to appropriately develop themselves.

5.4.2 Name and shame approach

South Africa has sufficient statutory and regulatory provisions (for example in the Companies Act and the *JSE Listing Requirements*)[644] which provide for the publication of delinquent directors' details but what has been lacking is effective implementation of these provisions. Therefore the government should vigorously implement a "name and shame" approach or public register of delinquent directors[645] which involves, *inter alia*, publicising the names of companies and directors that violate their fiduciary duties, frequently violate the provisions of the Companies Act, fail to publish annual accounts on time and in compliance with requirements and to observe listing and other stock exchange rules as well as those that are involved in insider dealing cases and payment of salary increases unmatched by productivity gains. The threat of reputational damage and publicity may be deterrent in that directors are less likely to risk financial harm or to compromise their reputations by engaging in unethical and unprofessional conducts. Implementation of the name and shame approach can be without much difficulty done through the Companies and Intellectual Property Commission[646] and the Johannesburg Stock Exchange who are strategically positioned to gather information on defaulting

[644] Section 69 of Act 71 of 2008 and section 1 of the *JSE Listing Requirements*.

[645] Section 162 of the Companies Act 71 of 2008 already provides for declaration of a director as delinquent so all that is needed is to effectively implement the provisions of the Act and to make public the names of the directors so declared.

[646] Established in terms of section 185 of the Companies Act 71 of 2008.

المنارة للاستشارات
www.manaraa.com

directors. The costs involved may not be so significant as the required information would be easily accessible and cheap publication means can be used.

However, there is also need to strengthen mechanisms to ensure that actions of directors are effectively monitored and evaluated thus translating the various codes of good practice into action as opposed to merely complying outwardly with codes of good corporate governance. Important to all of this, is the need for governing structures to engage in comprehensive periodic evaluations of the directors with the aim of assessing whether each director continues to contribute effectively and to demonstrate commitment to their duties. The results of the performance evaluation should assist in recognising the strengths and addressing the weaknesses of the directors and, where appropriate, proposing new members to be appointed or seeking the resignation of directors. Performance evaluation would also enable companies to detect and remove delinquent directors at the earliest opportunity without having to wait to effect the "name and shame" strategy.

5.4.3 Improve Enforcement Mechanisms

Although South Africa has upgraded its commercial laws to standards that are generally acceptable at an international level, even more importantly, it must make those laws fully effective, particularly through strengthening its court systems, tackling corruption, increasing awareness by directors of their responsibility and adopting appropriate measures to strengthen the rule of law. Consequently, the main emphasis during the next few years should be on improving the practical application of the existing corporate governance framework, not on introducing major new corporate governance initiatives. The other challenge for the future is to ensure that the South African model of corporate governance remains an asset rather than a liability for the country's business community.

South Africa has thus to focus more on improving the quality of its legal framework and enforcement mechanisms of existing laws and regulations. It has to equip, among others, the judicial system, regulatory bodies like the JSE, Financial Services Board, the office

المنارة للاستشارات
www.manaraa.com

of the Registrar of Companies and the Companies and Intellectual Property Commission to enforce the provisions of the Companies Act, investigate alleged breach of the provisions of the Companies Act and to monitor the progress of enforcement of corporate governance regulations and guidelines. What all this means is that supervisory, regulatory and enforcement authorities should have the authority, integrity and resources to fulfil their duties in a professional and objective manner. Moreover, their rulings should be timely, transparent, fully explained and deterrent enough. Whilst adequately resourcing and equipping all its judicial system and regulatory authorities might not be possible in the immediate future because of the need to address other social obligations, gradual attention to this noble cause should see the country significantly improving the quality of its enforcement to match international standards. Improved enforcement mechanisms should deter directors from breaching their fiduciary duties, abusing their powers and accessing excessive remuneration for fear of being penalised.

5.4.4 Encourage Shareholders Participation

Another observation from the research is that, although there is sufficient legislation to promote effective participation of shareholders, shareholder activism has not reached desirable standards.[647] South Africa should therefore, focus on intensifying constructive dialogue between directors and shareholders through rigorous educational campaigns[648] and encouragement of shareholders[649] so that they effectively participate in the business of their companies and also act as monitors of the directors to avoid situations where directors act unscrupulously and go unnoticed for too long until things get out of hand. Another important reason to note is that, without shareholder involvement, there is the risk that government will perceive a corporate governance vacuum, and transfer responsibility for corporate governance enforcement from shareholders to regulators.

[647] Chapter 3 paragraph 3.2.3.

[648] The government can consider supporting the development of shareholder associations which will coordinate educational campaigns, circulate information to shareholders and encourage shareholder participation at meetings.

[649] As a way of encouraging shareholders participation the policy makers can consider imposing some form of penalties on shareholders who fail to attend shareholders' meetings or to exercise any due right without any reasonable justification.

المنارة للاستشارات
www.manaraa.com

This would also reduce the flexibility of the South African model of corporate governance and impose unnecessary additional compliance costs on the country's companies. It is therefore important that the shareholders are educated to appreciate their role in ensuring that the companies in which they will have invested their monies are properly governed. If shareholders are adequately informed of their importance as a checking mechanism in safeguarding their investments, it would be easier to encourage them to participate in shareholders' meetings and any other relevant forum.

5.4.5 Enhance the effectiveness of non-executive directors

Non-executive directors are an essential part of the South African corporate governance approach, particularly for companies which lack substantial shareholder engagement. However, non-executive directors often have insufficient time and company-specific knowledge to effectively challenge executive directors. In order to reduce their information asymmetry vis-à-vis executive directors, non-executive directors thus need to be afforded access to resources and logistical support. Mechanisms should accordingly be put in place to enable them to obtain information independently so that they do not have to rely solely on executive directors for information and analysis.

Furthermore, non-executive directors need to be encouraged to attend professional training and development programmes to enable them to improve their effectiveness and manage their risks. It should not be practically difficult to train non-executive directors as reasonably cheap methods of training can be used. Although it is alleged that there are limited directors' skills in South Africa, the effectiveness of non-executive directors can also be enhanced by empowering them through formation of committees that consist mostly of non-executive directors so that their decisions are not overruled by the executive directors. To add to the above, non-executive directors can also be made more

المنارة للاستشارات
www.manaraa.com

effective if they are empowered to independently access certain key information to enable them to make sound decisions.[650]

5.4.6 Develop Guidelines on Executive Remuneration

A number of challenges seem to surround the issue of directors' remuneration. One such challenge is that, many business entities have not bothered to put remuneration committees in place and where the committees have been formed they are not very effective.[651] Therefore, one recommendation that comes easily is that there is need for educating boards of directors and shareholders to appreciate the importance of remuneration committees if directors' remuneration is to be linked to company performance. It is also entirely appropriate for shareholders to increase their engagement with companies over remuneration[652] so as to ensure that directors' remuneration matches production. If necessary, they should make more effective use of their voting rights if they believe that levels of director remuneration are not consistent with long-term value generation.

South Africa should promote establishment of institutions that produce guidelines[653] on remuneration to assist in the implementation of the principles and provisions of the *King Code* and other remuneration laws or regulations in place. However, it is important to appreciate the risks associated with implementing rigid remuneration policies which might negatively affect South Africa's competitiveness and distort the allocation of resources within enterprises. The guidelines and regulations should also not stifle the

---

[650] As an example, non-executive directors can be empowered to obtain information directly from certain company employees (for example internal audit).

[651] Chapter 2 paragraph 2.2.6.2.1.

[652] The companies Act already gives shareholders authority to participate in the determination of certain remuneration of directors for example section 45 of Act 71 of 2008. Similarly Chapter 2 of *King III* also recommends that the board should determine the remuneration of executive directors in accordance with the remuneration policy put to shareholder's vote.

[653] There are a number of Human Resources Consultancy firms that carry out salary surveys and these could be encouraged to publicise such information for the benefit of companies that may not have the capacity to carry out the surveys on their own.

المنارة للاستشارات
www.manaraa.com

company's ability to attract and retain directors, nor should they discourage robust yet responsible entrepreneurship and risk-taking. The guidelines should thus be used only as a guiding tool without imposing a financial burden on companies and introducing rigidity. As long as remuneration is performance based challenges of excessive remuneration will be eliminated as well-performing directors will produce good results for their companies and will thus be highly rewarded. Likewise, non-performers will produce poor results which in turn mean poor remuneration for the directors. After all is said and done the bottom line is that performance targets should be set for directors and their remuneration should be based on achievement of the set targets and approval by shareholders.

5.4.7 Improve quality of information in accounts and reports

The research revealed that there are adequate laws and regulations that require directors to disclose certain information in the company's financial statements and annual reports but what is needed is to improve on the quality of the information so disclosed.[654] It is therefore, recommended that the relevant and reliable corporate governance information that is disclosed in the company's financial statements and annual reports should be comprehensive enough to enable users and stakeholders to make informed decisions on the basis of information. Where the company cannot make a required disclosure the explanation for non-disclosure should indicate the estimated timeframe within which it is targeted to comply with the disclosure requirements. This should make it easier for users and stakeholders to determine when to expect that the directors will have addressed the non-disclosure.

To add to this there is need to develop guidelines on how whistle blowing information can be reflected in annual reports to enable stakeholders to get to know the rate and nature of fraudulent activities experienced by the company which might be useful in assessing risk. Implementing this recommendation should not present major difficulties as directors who fail to comply could be penalised as well as publicised. For fear of

[654] Chapter 3 paragraph 3.2.5.

المنارة للاستشارات
www.manaraa.com

reputational damage most of the directors should comply. Audits reports on the financial statements also present another checking mechanism on poorly presented statements.

المنارة للاستشارات
www.manaraa.com

BIBLIOGRAPHY

Books

Beuthin R C & Luiz S M, *Beuthin's Basic Company Law,* 3rd Edition (2000).

Breadly R A & Myers, *Principles of Corporate Governance*, 7th Edition (2004).

Bruce M, *Rights and Duties of Directors,* 8th Edition (Tolley's 2006).

Campbell D & Woodley S, *Trends and Developments in Corporate Governance,* (Kluwer Law International 2003).

Cilliers H.S, Benade M.L, Henning J.J, Du Plessis J.J, Delport P.A, De Koker L, Pretorius J.T, *Corporate Law*, 3rd Edition, (Butterworths 2000).

Colley, Jr., J.L; Doyle J.L; Logan G.W. & Stettinius W, *Corporate Governance*, (McGraw-Hill 2003).

Coyle B, *Corporate Governanc*e, (ICSA Publishing Ltd 2003).

Davis D, Cassim F, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L, Burdette D, *Companies and Other Business Structures in South Africa*, (Oxford University Press Southern Africa (Pty) Ltd. 2009).

Davies P. L, *Gower's Principles of Company Law*, 6th Edition (London: Sweet & Maxwell 1997).

Delport P, *The New Companies Act Manual*, (LexisNexis 2009).

Emery D R, Finnerty J D and Stowe J D, *Corporate Financial Management*, 2nd Edition (Upper Saddler River 2004).

Farrar J H & Hannigan B M, *Farrar' Company law*, 4th Edition (Butterworths 1998).

Hamann R, *South Africa: The Role of History, Government and Local Context*, (Springer Berlin Heidelberg 2009).

King M, *Governance for all Entities,* The Corporate Citizen (Penguin Books 2006).

Lipman F D. & Lipman L K, *Corporate Governance Best Practices: Strategies for Public, Private, and Not-for-Profit Organizations*, (John Wiley & Sons 2006).

Mallin C A, *Handbook on International Corporate Governance: Country Analyses*, (Edward Elgar Publishing 2006).

Maassen G F, *An international Comparison of Corporate Governance Models*, 3rd Edition (Gregory Maassen 2002).

المنارة للاستشارات
www.manaraa.com

Mammatt J, Du Plessis D & Everingham G, *The Company Director's Handbook*, (Siber Ink 2004).

Naidoo R, *Essentials for Corporate Governance for South African Companies,* (Double Storey 2002).

Pretorius J T, Delport P A, Havenga M and Vermas M, *Hahlo's South African Company Law Through the Cases*, 6th Edition (Juta & Co, Kenwyn 1999).

Smit P J, *Management Principles: A Contemporary Edition for Africa*, (Juta & Co. 2007).

Van der Merwe J G, Appleton R B, Delport P A, Furney R N, Mahony D P, Koen M, *South African Corporate Business Administration*, (Juta & Co Ltd 2009).

Van Dorsten J, *The Law of Company Directors in South Africa,* (Meridian Press CC 1999).

Wixley T. & Everingham G, *What You Must Know About Corporate Governance*, (Siber Ink CC 2002).

Wixley T and Everingham G, *Corporate Governance*, 2nd Edition (Siber Ink CC, 2005).

Cases

African Claim and Land Co. Ltd v W J Langermann 1905 TS 494.

Automatic Self-Cleansing Filter Syndicate Co v Cunningham [1906] 2 Ch 34.

Bairstow v Queens Moat Houses plc [2000] 1 BCLC 549 (QBD).

Da Silva & others v C H Chemicals (Pty) Ltd 2008 (6) SA 620 (SCA).

Dorchester Finance Co v Stebbing [1989] BCLC 498.

Du Plessis NO v Phelps (1995 (4) SA 165 (C).

Du Plessis v Phelps 1995 4 SA 165 (C) 171.

Fisheries Development Corporation of SA Ltd v Jorgensen & Another; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd & Others (1980 (4) SA 156 (W) 156).

Henway Freight Services (Pty) Ltd v Grogor 2007 (2) SA 561 (SCA).

Howard Smith Ltd v Ampol Petroleum Ltd [1974] AC 832.

Hogg v Cramphorn Ltd [1967] Ch. 254.

Magnus Diamond Mining Syndicate v Macdonald and Hawthorne 1909 ORC 65

Multi Tube Systems (Pty) Ltd v Ponting and Others 1984 (3) SA 182 (D).

Minister of Water Affairs and Forestry V Stilfontein Gold Mining Co Ltd and Others 2006 (5) SA 333 (W)

www.manaraa.com

Phillips v Fieldstone Africa (Pty) Ltd, 2004 (3) SA 465 (SCA).

Philotex (Pty) Ltd & Others v Snyman & Others 1998 (2) SA 138 (SCA).

Robinson v Randfontein Estates Gold Mining Company Limited 1921 (AD) 168.

Re Brazilian Rubber Plantations and Estates Ltd (1911) 1 Ch 425.

Re City Equitable Fire Insurance Co [1925] Ch 407 429.

Re National Bank of Wales Ltd ([1899] 2 Ch 629 (CA).

Regal (Hastings) Ltd v Gulliver [1942] All ER 378.

Royal British Bank v Turquand (1856) 6 E&B 327.

Shaw & Sons (Salford) Ltd v Shaw [1935] 2 KB 113.

Sibex Construction (SA) (Pty) Ltd v Injectaseal CC 1988 (2) SA 54 (T).

Symington v Pretoria-Oos Privaat Hospitaal Bedryfs (Pty) Ltd 2005 (5) SA 550 (SCA).

Swerdlow v Cohen 1977 (1) SA 178 (W) 182E-G.

Turquand v Marshall ([1869] LR 4 App 376 (Ch D)).

Theses

Esser I, *Recognition of Various Stakeholder Interests in Company Management*, Published LLD Thesis, (UNISA 2008).

Horn R. C, The *Legal Regulation of Corporate Governance with Reference to International Trends*, Published LLM Thesis, (University of Stellenborsh 2005).

Moloi S T M, *Assessment of Corporate Governance Reporting in the Annual Reports of South African Listed Companies*, Published MSc Thesis, (UNISA 2008).

Tumuheki J**,** *Towards Good Corporate Governance: An Analysis of Corporate Governance Reforms in Uganda,* Published MSc Thesis, (University of Cape Town 2008).

Journals

Armstrong P, Segal N and Davis B, Corporate Governance: South Africa, a Pioneer in Africa, *Global Best Practice, Report No. 1, The South African Institute of International Affairs*, Johannesburg, (2005).

Bainbridge S M, The Business Judgment Rule as Abstention Doctrine, (2004) *Vanderbilt Law Review,* Vol. 57(1).

المنارة للاستشارات
www.manaraa.com

Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the Nineteenth Century to the Companies Bill of 2007, (2008) 20 *South African Mercantile Law Journal* 95–116.

Berg A, The Company Law Review: Legislating Directors' Duties, (2000) *Journal of Business Law* 472.

Bosch H, The Changing Face of Corporate Governance, (2002) *University of New South Wales Law Journal*, Vol. 25(2) 270-293.

Carmody P, Between Globalisation and (Post) Apartheid: the Political Economy of Restructuring in South Africa, (2002) *Journal of Southern African Studies*, Vol.8(2) 1465-3893.

Cassim M F, Da Silva v C H Chemicals (Pty) Ltd: Fiduciary Duties of Resigning Directors, (2009) *The South African Law Journal*, Vol. 126(1), 61-70,.

Clieaf V, Executive Accountability and Excessive Compensation: a New Test for Director Liability, (2004) *The Corporate Governance Advisor* 12(6).

Clinch G & Verrechia R E, Competitive Disadvantage and Discretionary Disclosure in Industries, (1997) *Australian Journal of Management*, 22 (2), 125-138.

Conrad R and Holtzhausen J, King II, Corporate Governance and Shareholder Activism, (2003) *SALJ,* Vol. 120 (4), 767-776.

Cunningham G M & Harris J E, Enron and Arthur Andersen: The Case of the Crooked E and the Fallen A, (2006) *Global Perspectives on Accounting Education* Vol. 3(1), 27-48.

DeJong A, DeJong D. V, Mertensa G, Wasley C, The Role of Self-Regulation in Corporate Governance: Evidence and Implications from The Netherlands, (2005) *Journal of Corporate Finance* 11, 473–503.

Du Plessis J J, Corporate Governance and the Cadbury Report, (1994) 6 *South African Mercantile Law Journal* 81, 82.

Esser I & Dekker A, The Dynamics of Corporate Governance in South Africa: Broad Based Black Economic Empowerment and the Enhancement of Good Corporate Governance Principles, (2008) *Journal of International Commercial Law and Technology,* Vol. 3(3).

Ferran E, The Decision of the House of Lords in Russel v Northern Bank Development Corporation Ltd, (1994) *Cambridge Law Journal*, Vol. 53(2) 343-366.

Finch V, Company Directors: Who Cares about Skill and Care? (1992) 55 *Modern LR*179 179.

Fisch J E and Rosen K M, Is there a Role for Lawyers in Preventing Future Enrons? (2003) *Villanova Law Review*, Vol. 48, 1097-99.

Havenga M, Breach of Directors' Fiduciary Duties: Liability on What Basis? (1996) 8 *South African Mercantile Law Journal* 366.

Havenga M, Directors in Competition with Their Companies, (2004) *South African Mercantile Law Journal* 275.

المنارة للاستشارات
www.manaraa.com

Havenga M K, Directors' Fiduciary Duties under our Future Company Law Regime, (1997) 9 *South African Mercantile Law Journal* 310- 324.

Havenga M, The Business judgement Rule- Should we Follow the Australian Example? (2000) *South African Mercantile Law Journal* 36.

Jensen M and Meckling W, Theory of Firm: Managerial Behavior, Agency Costs and Ownership Structure, (1996) *Journal of Economics*.

Jesover F & Kirkpatrick G, The Revised OECD Principles of Corporate Governance and their Relevance to Non-OECD Countries, (2005) *Corporate Governance: An International Review*, Vol. 13 (2).

Kiggundu J & Havenga M, The Regulation of Directors' Self-serving Conduct: Perspectives from Botswana and South Africa, (2004) *Comparative and International Law Journal of Southern Africa,* Vol. 37(3).

La Porta R, Lopez-de Silanes F, Shleifer A and Vishny R, Investor Protection and Corporate Valuation, (2002) *Journal of Finance* 57.

Mackenzie A. L, A Company Directors' Obligations of Care and Skill, (1982) *Journal of Business Law* 460.

Mallette, P, State Anti-corporate Takeover Laws: Issues and Arguments, (1995) *Journal of Managerial Issues*.

O'Donovan G, A Board Culture of Corporate Governance, (2003) *Corporate Governance International Journal*, Vol. 6 (3).

Point S and Tyson S, Top Pay Transparency in Europe: Codes, Convergence and Clichés, (2006) *The International Journal of Human Resources Management*, Vol. 17 (5).

Rademeyer C and Holtzhausen J, King II, Corporate Governance and Shareholder Activism, (2003) *SALJ, Vol*. 120 (4).

Rafael La Porta, Florencio Lopez De Silanes, Andrei Shleifer, and Robert Vishny, Legal Determinants of External Finance, (1997) *The Journal of Finance* 52.

Rosenthal A J, Remedies in Disputes Arising Out of Agreements to Buy and Sell Businesses, (1971) *Boston College Law Review,* Vol 12(5) 836-842

Rossouw G. J, Van der Watt A, Malan D. P, Corporate Governance in South Africa, (2002) *Journal of Business Ethics* 37, 289–302.

Salacuse J W, Corporate Governance in the New Century, (2004) *The Company Lawyer* 25(3).

Sher H, Company Directors' Duties and Responsibilities, (2005) *Juta's Business Law,* Vol 13(3) 129-131.

Shil, N. C, Accounting for Good Corporate Governance, (2008) *JOAAG*, Vol. 3(1).

Stuart Cohn, Teaching in a Developing Country: Mistakes Made and Lessons Learned in Uganda, (1998) *Journal Legal Education* 48, 101-104.

المنارة للاستشارات
www.manaraa.com

Trebeck K, Exploring the Responsiveness of Companies: Corporate Social Responsibility to Stakeholders, (2008) *Social Responsibility Journal*, Vol. 4(3) 349-365.

Van Der Linde K, The Personal Liability of Directors for Corporate Fault –An Exploration, (2008) 20 *South African Mercantile Law Journal* 439–461.

Van Melle Kamp C, Corporate Governance in Africa –The Impact on Non-Executive Directors, (2005) *Professional Management Review*, 16 (9).

Vaughn M, Verstegen Ryan & Lori J, Corporate Governance in South Africa: A Bellwether for the Continent? *Corporate Governance: An International Review*, (2006) Vol. 14 (5).

Reports

Cadbury Report, 1992 (United Kingdom).

Combined Code, 2003 (United Kingdom).

OECD Principles of Corporate Governance, (OECD, April 1999).

Greenbury Report, 1995 (United Kingdom).

King I Report on Corporate Governance for South Africa, 1994 (South Africa).

King II Report on Corporate Governance for South Africa, 2002 (South Africa).

King III Report on Corporate Governance for South Africa, 2009 (South Africa).

Report of the Securities and Exchange Board of India (SEBI) Committee on Corporate Governance (India).

Statutes and Acts

Broad-based Black Economic Empowerment Act 53 of 2003 (South Africa).

Companies Act 61 of 1973 (South Africa).

Companies Act 71 of 2008 (South Africa).

Companies Act, Cap. 46 of 2006 (United Kingdom).

Company Directors (Disqualification) Act of 1986 (United Kingdom).

Department of Trade and Industry (DTI) Policy Document (United Kingdom).

Insider Trading Act 135 of 1998 (South Africa).

Municipal Finance Management Act 56 of 2003 (South Africa).

Public Finance Management Act 1 of 1999 (South Africa).

المنارة للاستشارات
www.manaraa.com

Securities Services Act 36 of 2004 (South Africa).

The Draft Companies Bill, 2007 (South Africa).

The Directors' Remuneration Report Regulations 2002 (United Kingdom).

Explanatory Memorandum to the South Africa Companies Bill, 2007.

South African Company Law for the 21st Century, Guidelines for Corporate Law Reform announced by the Minister of Trade and Industry, May 2004.

Internet sources

American Bar Association (ABA), *Report of the Task Force on Corporate Responsibility*, February 2002, available at: http//www.abanet.org/buslaw/corporateresponsibility/finalreport.pdf.

Cahn N, *Corporate Governance Divergence And Sub-Saharan Africa: Lessons From Out Here In The Fields,* available at justice.law.stetson.edu/lawrev/abstracts/PDF/33-3Cahn.pdf .

Clive D K, *King II Report on. Corporate Governance 2002: Summary of Code of Corporate Practices and Conduct*, available at www.rtmc.co.za/.../king%20ii%20report%20summary%20of%20code.pdf.

Commonwealth Association for Corporate Governance. *CACG Guidelines: Principles for Corporate Governance in the Commonwealth*. (1999), available at http://www.ecgi.org/codes/code.php?code_id=24.

Cooper M. S, *Corporate Governance In Developing Countries: Shortcomings, Challenges & Impact on Credit,* Paper presented at the Congress to celebrate the fortieth annual session of UNCITRAL Vienna, 9-12 July 2007, available at www.uncitral.org/pdf/english/congress/Cooper_S_rev.pdf.

Deloitte, *Guide to the JSE Listings Requirements*, available at www.deloitte.com/assets/.../JSE%20Listings%20Requirements.pdf.

Deloitte, *Report on the impact of Directors' Remuneration Report Regulations*, A Report for the Department of Trade and Industry, available at www.berr.gov.uk/files/file13425.pdf.

Deutsche Bank Securities Incorporated, Global Corporate Governance, *Valuing Corporate Governance in South Africa*, August 19, 2002 available at www.ifc.org/ifcext/corporategovernance.../DB+on+South+Africa.pdf.

Eisenberg M A, *The Duty of Care in American Corporate Law*, Institute for Law and Finance, Working Paper Series No. 22 (2004) available at http://www.ilf-frankfurt.de/uploads/media/ILF_WP_022.pdf.

Estandardsforum Financial Standards Foundation, Report on South Africa, *Principles of Corporate Governance,* at www.estandardsforum.org/servlet.

المنارة للاستشارات
www.manaraa.com

Falkena H, Bamber R, Llewellyn D and Store T, Financial Regulation in South Africa, *SA Financial Sector Forum,* (2001) available at http://www.finforum.co.za/publications/fregall.pdf (visited on 12 November 2009).

Ferri F& Maber D, *Say on Pay Vote and CEO Compensation: Evidence from the UK*, (Harvard Business School 2008), available at http://69.175.2.130/~finman/Reno/Papers/FMASayOnPay.pdf.

Financial Reporting Council, *The UK Approach to Corporate Governance*, (2006) available at http://www.frc.org.uk/documents/pagemanager/frc/FRC%20The%20UK%20Approach%20to%20Corporate%20Governance%20final.pdf.

CGF Research Institute (Pty) Ltd, *Directors' Code May Steer Corporate Governance into a Common Law Storm, November 2007*available at http://www.cosecs.co.za/editorial/01%20Nov%2007%20-%20Directors%20code%20may%20steer%20governance%20into%20common.pdf.

CGF Research Institute, *The Case For Good Governance - Past, Present And Future*, available at www.Irca.Co.Za/Docs/14_May_09_The_Case_For_Good_Governance.Pdf.

Grant Thornton South Africa, *JSE Listings Requirements*, at http://www.gt.co.za/Publications/Effective-directors-guide/jse.asp.

Grant Thornton South Africa, *Directors' Duties, Responsibilities and Rights,* available at: http://www.gt.co.za/Publications/Effective-directors-guide/directors_duties.asp.

Havenga M, *Regulating Conflicts of Interest and South African Company Law Reform,* UNISA, available at http://www.law.usyd.edu.au/parsons/CLTA/HavengaPaper.pdf

Havenga M, *Regulating Directors' Duties & South African Company Law Reform*,(UNISA) available at www.sabinet.co.za/abstracts/obiter/obiter_v26_n3_a13.xml.

Institute for Security Studies, *Why Ethics Regulations Continue to Fail SA,* available at http://www.polity.org.za/article/why-ethics-regulations-continue-to-fail-sa-2009-09-02.

Institute of Chartered Secretaries and Administrators of South Africa, *Codification,* Presentation to the Department of Trade and Industry on the Draft Companies Bill, March 2007 available at available at http://www.icsa.co.za/assets/presentations/companiesbill/final.pdf.

Institute of Chartered Accountants in England and Wales, *Corporate Governance Developments in the UK*, available at http://www.icaew.com/index.cfm/route/149243/icaew_ga/en/Technical_and_Business_Topics/Topics/Corporate_governance/Corporate_governance_developments_in_the_UK.

JSE Securities Exchange South Africa Listing Requirements available at http://www.jse.co.za/ listing_requirements.jsp.

Keynote Address by Tshediso Matona, Director-General: Trade and Industry, *Conference on South African Company Law for the 21st Century*, Pretoria, 19 March 2007 available at www.info.gov.za/speeches/2007/07032013451001.htm.

المنارة للاستشارات
www.manaraa.com

Langtry S, *Corporate Governance,* A Discussion Paper to Assist with the Preparation of South Africa's African Peer Review Mechanism (APRM) Self Assessment Report, *(*2005) available at www.aprm.org.za/docs/APRMOpinionPiece-Corporate _Governance.

Leong Ho Khai, *Reforming Corporate Governance in Southeast Asia: Economics, Politics and Regulations,* Institute of Southeast Asia Studies (ISEAS) Singapore, (2005) available at *www3.ntu.edu.sg/.../HoKhaiLeong/Ho%20Khai%20Leong%20vita%20October%202007.pdf*.

Loubser R, *Insider Trading and Other Market Abuses (Including the Effective Management of Price Sensitive Information)* available at http://www.jse.co.za/Libraries/JSE_-_

Mcgregor L – *Improving Corporate Governance in South Africa,* Discussion paper submitted for the 1st USB Colloquium on Corporate Governance, 18th September 2008 available at http://www.governance.usb.ac.za/downloads/UnitColloquiumPaper1_LynnMcGregor.pdf.

Malherbe S and Segal N, *Corporate Governance in South Africa*, Paper prepared for the OECD Development Centre, (2001) available at www.estandardsforum.org/south-africa/.../principles-of-corporate-governance.

McKinsey and Company, *Investor Opinion Survey on Corporate Governance* (June 2000), available at www.oecd.org/dataoecd/56/7/1922101.pdf.

Müller N, *Financial Services Board Report* (2005) available at ftp://ftp.fsb.co.za/public/documents/AReport08_2005.pdf.

New Partnership for Africa's Development (NEPAD), *African Peer Review Mechanism: Country Review Report of South Africa, September 2007*, (NEPAD 2007) at http://www.aprm.org.za/docs/SACountryReviewReport5.

OECD*, Lack Of Proportionality Between Ownership And Control: Overview And Issues for Discussion*, Paper Issued by the OECD Steering Group On Corporate Governance, December 2007, available at http://www.oecd.org/dataoecd/21/32/40038351.pdf.

Okeahalam C.C and Akinboade O.A, *A Review of Corporate Governance in Africa: Literature, Issues and Challenges*, paper presented for the Global Corporate Governance Forum on 15 June 2003 available at http://www.ifc.org/ifcext/cgf.nsf/AttachmentsByTitle/Pan_Africa_2003_Review_of_CG_Okeahalam/$FILE/Charles+Okehalam+-+Corporate-Governance+ver+4+Jul+2003.pdf.

Plumptre T, *The New Rules of the Board Game*, *The Changing World of Corporate Governance and its Implications for Multilateral Development Institution*, Institute on Governance, Ottawa, (2004), available at www.iog.ca.

Prasanna P K, *Corporate Governance and Directors Remuneration*, The Chartered Accountant May 2005 available at http://icai.org/resource_file/10641may05p1483-89.pdf.

PricewaterhouseCoopers (PwC), *Corporate Governance in South Africa: A Comparison of the King Report 2002 and The Sarbanes-Oxley Act of 2002*, (2002) PriceWaterhouseCoopers, available at http://www.pwcglobal.com/za/eng/inssol/.

المنارة للاستشارات
www.manaraa.com

PricewaterhouseCoopers Southern Africa, *Corporate Governance- An Executive Guide to King III,* available at www.complianceweek.com/s/documents/south-africa-report.pdf.

PricewaterhouseCoopers, *Draft King III at a Glance*, available at www.iodsa.co.za/.../Draft%20King%20III%20at%20a%20glance.pdf.

PricewaterhouseCoopers (PwC), *Non-executive Directors: Increased Responsibility and a Shrinking Pool of Talent,* (Johannesburg 2008), available at www.iodsa.co.za/downloads/.../07-03171-directors%20brochure.pdf.

Report of the SEBI Committee on Corporate Governance, February 2003, available at http://www.acga-asia.org/public/files/India_MurthyCtee_Feb03.pdf.

Sarra, J. P. (2004), *Strengthening Domestic Corporate Activity in Global Capital Markets: A Canadian Perspective on South Africa's Corporate Governance*, The George Washington University Law School Public Law and Legal Theory Working Paper No 118, Institute for International Corporate Governance and Accountability, 29 available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=628702.

Securities Exchange Commission, *SEC Charges Kenneth L Lay, Enron's Former Chairman and CEO with Fraud and Insider Trading*, 2004, available at http//www.sec.gov/news/press/2004-94.htm.

Terry Booysen, *The Case For Good Governance - Past, Present And Future,* CGF Research Institute, 14 May 2009, available at www.cgfresearchinstitute.com/LinkClick.aspx?fileticket.

The Department of Trade and Industry and King's College London, *Key Drivers of Good Corporate governance and the Appropriateness of UK Policy Responses,* (2007), available at http://www.berr.gov.uk/files/file36671.pdf.

The Organization of Economic Cooperation and Development Principles of Corporate Governance available at www.oecd.org.

The Transparency International 2009 Corruption Perceptions Index (CPI) available at http://www.guardian.co.uk/news/datablog/2009/nov/17/corruption-index-transparency-international.

The UK Companies Act, 2006, Regulatory Impact Assessment, January 2007. available at http://www.dti.gov.uk/files/file29937.pdf.

Tim Plumptre, *The New Rules of the Board Game*, *The Changing World of Corporate Governance and its Implications for Multilateral Development Institution*, Institute on Governance, Ottawa, (2004), available at www.iog.ca.

The United Kingdom Explanatory Notes to the Companies Act, available at the Department of Trade and Industry website at http://www.dti.gov.uk.

United Nations Conference on Trade and Development, *Guidance on Good Practices in Corporate Governance Disclosure,* United Nations, New York and Geneva, 2006 available at: http://www.unctad.org/en/docs/iteteb20063_en.pdf.

المنارة للاستشارات
www.manaraa.com

UK Institute of Directors, *The UK Model of Corporate Governance: An Assessment from the Midst of a Financial Crisis*, available at http://www.iod.com/intershoproot/eCS/Store/en/pdfs/policy_publication_The_UK_Model_of_Corporate_Governance.pdf.

Vallet P, Girard M and Phalane J, *Overview of Recent Corporate Governance Reforms, South Africa*, Fluxmans Inc available at http://www.globalcorporategovernance.com/n_africa/316_322.htm.

Wymeersch E, *Corporate Governance Codes and their Implementation,* Ghent University Financial Law Institute Working Paper No. 2006-10, available at *papers.ssrn.com/sol3/papers.cfm?abstract_id=931100&rec=1.*

Newspapers

Marcotti A. G, *Fiduciary Duty and Directors' Pay,* The Times, 13 March 2009.

Maimonis A, *Rule-Focus Ed Approach Makes Corporate Governance a Snag,* Businessday, 17 September 2009.

للاستشارات المنارة

www.manaraa.com