Directors’ Fiduciary Duties Under Our Future Company-law Regime*

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1 Introduction

As a separate legal entity or juristic person which exists apart from its management and shareholders, a company must necessarily act through individuals.1 The functions and responsibilities of corporate directors, who are entrusted with its management,2 arise by virtue of this nature of a company. Company management can only be effective if those who manage are allowed a certain measure of freedom and discretion in the exercise of their function. Contrarily, effective control of management is vital in the interests of the company itself and its various stakeholders. This philosophy underpinning corporate governance is illustrated by the recognition by the King Committee that in the context of corporate governance, a proper balance needs to be established between freedom to manage, accountability and the interests of the different stakeholders.3 Company directors are therefore subject to various duties. Their onerous common-law fiduciary responsibilities exist in addition to the various statutory duties contained in the Companies Act,4 their obligations of care and skill, and any duties which a company’s articles of association or a separate agreement may specify. South African company law has always relied heavily on the English law for the formulation of legal principles in this respect. This is not surprising, since not only is the incorporated company of our law modelled after its English counterpart,5 but the

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2 Although the Legislature places no obligation on companies to assign any particular task to the board of directors, it exists conceptually to undertake the management of the company, or, at the least, to assume responsibility for it: Cilliers et al op cit note 1 at 133; MS Blackman ‘Companies’ in: WA Joubert (ed) The Law of South Africa vol 4(1) (1995) par 161. Thus, it is usual for the articles to provide that the business of the company shall be managed by the directors (see art 59 of Table A and art 60 of Table B in Schedule 1 of the Companies Act 61 of 1973).
5 See Elmarie de la Rey ‘Aspekte van die Vroeë Maatskappyreg: ‘n Vergelykende Oorsig’ (1986) 4 Codicillus 18ff; SJ Naude Die Regsposisie van die Maatskappydirekteur met Besondere
fiduciary obligation, as a legal principle, also originated in that system. The company laws of Australia, New Zealand and Canada are, however, becoming of increasing comparative value as a consequence of the harmonisation of company laws between England and the other member states of the European Union, some of which do not recognise a fiduciary relationship between directors and their companies.

A company directorship is generally regarded as one of the most complex fiduciary offices. The fiduciary relationship arises from the purpose for which the director's office and powers are entrusted to her, namely the benefit of the company. In order to facilitate their evaluation, it is common practice to categorise specific fiduciary duties, such as the duties to act with an unfettered discretion, in good faith, in the interests of the company as a separate legal entity, within the limits of the power conferred upon the particular director, and to avoid a conflict of interest and duty. These categories are not exclusive and, to some extent,

Verweyse na die Interne Maatskappyverband (1970) at 9; Hahlo's South African Company Law Through the Cases: A Source Book 5 ed by JT Pretorius (gen ed), PA Delporte, Michele Havenga & Maria Vermaas (1991) at 1–3; Ex parte Provisional Liquidator Hugo Franco (Pty) Ltd 1958 (4) SA 397 (W) at 399H–400D.


7 The company laws of Australia, Canada and New Zealand are based on English law. However, all three countries have recognised the need to deviate from that system. Moreover, their company laws have recently been reformed. The laws of these three Commonwealth countries are influential with regard to developments in South African company law, especially in view of the fact that South Africa has been readmitted to the Commonwealth.

8 Finn op cit note 6 at 64. JC Shepherd The Law of Fiduciaries (1981) at 347–348 agrees: 'Nowhere are fiduciary principles applied in a more difficult or complex context than the modern corporation — any attempt to build tiny little cubbyholes in the corporate context is doomed to failure'. The problem in South African law too, is that no specific interpretation can be attributed to the term 'fiduciary duty'. This leads to vagueness and gives rise to uncertainty which in turn leads to ineffectiveness of the prophylactic aim of strict fiduciary responsibilities imposed on directors: see JJ du Plessis Maatskappyeconomie van die Bedryfsgelyke Verband (unpublished PhD thesis, University of the Orange Free State (1990)) at 88–93 and 100–109; JJ du Plessis 'The Duties of Directors with Special Reference to Deposit-taking Institutions' 1993 J of South African Law 56 at 57.

9 For example, LCB Gower Gower's Principles of Modern Company Law 5 ed (1992) at 553 distinguishes four rules which have emerged from the application of the general equitable principle to company directors. Directors must act in good faith in what they believe to be the best interests of the company. They must not exercise the powers conferred upon them for purposes different from those for which they were conferred and may not fetter their discretion as to how they shall act. Lastly, they may not, without the informed consent of their company, place themselves in a position in which their personal interests or duties to other persons are liable to conflict with their duties to the company. Robert R Pennington Company Law 6 ed (1990) at 583 and 584 distinguishes two main duties, namely the duty not to exceed powers and the duty to act in the interests of members and employees. John H Farrar, Nigel E Furey & Brenda M Hannigan Farrar's Company Law 3 ed (1991) at 383ff identify directors' duties to act bona fide in the interests of the company and not to exercise their powers for any collateral purpose. The authors of Corporate Law distinguish four categories, namely that directors (a) should prevent a conflict of interest; (b) may not exceed the limitations of their power; (c) must maintain an unfettered discretion; and (d) should exercise their powers for the purpose for which they were conferred: see Cilliers et al op cit note 1 at 137.
overlap.10 But they form part of one broad duty which requires that the director should act in good faith in the best interests of the company.11

In this discussion I will concentrate on two facets related to a director's fiduciary obligation, namely the effect that our Constitution may have on its assessment, and the beneficiary of the duty.

2 The Effect of the Constitution

The first aspect concerns the effect of our Constitution on the assessment of directors' fiduciary responsibilities.12 That the Bill of Rights contained in Chapter Two applies to non-statutory as well as statutory law, is clear from the wording of s 8(1) which provides that the Bill applies to all law, and binds the legislature, the executive, the judiciary and all organs of state. It is equally clear that all persons are bound by the Bill. Section 8(2) states that a provision of the Bill binds a natural or a juristic person if, and to the extent that, it is applicable, taking into account the nature of the right and the nature of the duty imposed by the right. This section also grants a court the right, when applying a provision of the Bill to a natural or a juristic person, to apply, or if necessary to develop, the common law to the extent that legislation does not give effect to that right, and to develop rules of the common law to limit the right, provided that the limitation is in accordance with the limitation provisions of the Bill.13 The lively debate about the possible horizontal application of the Bill of Rights contained in the interim Constitution14 was settled by the decision in Du Plessis & Others v De Klerk & Another15 where the Constitutional Court held that the Bill had at least indirect horizontal effect. This requires that that all legal rules

10 See Farrar op cit note 9 at 380n12.
11 See Blackman 'Fiduciary Doctrine' op cit note 6 at 285; RJ Calnan ‘Corporate Gifts and Creditors' Rights' (1990) 11 Company Lawyer 91 at 93; Corporate Law op cit note 1 at 156; Farrar op cit note 9 at 380; OJS Fourie ‘Die Plig van Direkteure teenoor Maatskappyskuldeisers’ (1992) 4 SA Merc LJ 25–26 and authorities cited in n12; Gower op cit note 9 at 553–556; Pennington Company Law op cit note 9 at 583; Geoffrey Morse (gen ed) Palmer's Company Law 25 ed vol I (1992) at 8104–8105; Leon van Rooyen Die Geldigheid van die Besluite van 'n Algemene Vergadering in die Maatskappyereg (unpublished LLD thesis, Rand Afrikaans University (1983)) at 325 and 363ff; Sarah Worthington 'Directors' Duties, Creditors' Rights and Shareholder Intervention' (1991) 18 Melbourne University LR 121; S v De Jager & Another 1965 (2) 616 (A); S v Shaban 1965 (4) SA 646 (W); S v Ressel 1968 (4) SA 224 (A); S v Heller 1971 (2) SA 29 (A) at 44; Novick & Another v Comair Holdings Ltd & Others 1979 (2) SA 116 (W) at 130 and 151; Timmers & Another v Spanco Welding (Pty) Ltd 1979 (3) SA 242 (T) at 251; Fisheries Development Corporation of SA Ltd v Jorgensen 1980 (4) SA 156 (W) at 163E–G; Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Gwano (Pty) Ltd & Others 1981 (2) SA 173 (T) at 198; and Sibex Construction (SA) (Pty) Ltd v Injectaseal CC & Others 1988 (2) SA 54 (T) at 65.
13 Section 8(3). The provisions in respect of the limitation of rights appear in s 36. The rights contained in the Bill may be limited only in terms of law of general application to the extent that the limitation is reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom, taking into account all relevant factors. The relevant factors include the nature of the right, the importance of the purpose of the limitation, its nature and extent, the relation between the limitation and its purpose, and less restrictive means to achieve the purpose.
14 The Bill of Rights is contained in Chapter Three (Fundamental Rights) of the Constitution of the Republic of South Africa, Act 200 of 1993.
must be interpreted in a manner that reflects the values underpinning the fundamental rights.\(^\text{16}\) The final Constitution provides for direct horizontal application in certain instances, for example in respect of the equality clause contained in s 9.\(^\text{17}\) Direct horizontal application implies that the Bill does not apply only to the relations between the state and its citizens, but also to private law relations between individuals.\(^\text{18}\) It seems that those clauses which do not have direct horizontal application, will have such application indirectly. The inevitable conclusion is that the legal rules pertaining to a director’s fiduciary relationship with her company must be interpreted in such a manner that it reflects the fundamental values of the Bill of Rights.

The duty to act in good faith is an example of a so-called open-ended standard, the interpretation of which depends on policy considerations.\(^\text{19}\) These policy considerations can, to a considerable extent, be extracted from the provisions of the Bill of Rights since it reflects the fundamental legal values accepted in our society. The standard of good faith required from a director must, in other words, be gauged in the light of the boni mores or legal convictions of the community as reflected in the Bill of Rights. In this regard, s 39(2) provides that when interpreting any legislation, and when developing the common law or customary law, every court, tribunal or forum must promote the spirit, purport and objects of the Bill of Rights. Specific rights conferred in the Constitution, for example the right to an environment that is not harmful to a person’s health and well-being,\(^\text{20}\) and the right not to be deprived of property,\(^\text{21}\) will also have to be considered.

I submit that public policy requires a model of corporate governance which is both legally justifiable and acceptable in our developing economic community. The emphasis in the concept of corporate social responsibility can be expected to change accordingly.\(^\text{22}\) Corporate social


\(^\text{17}\) See Havenga op cit note 16 at 277. See also Woolman & Davis op cit note 16 at 399ff who argue compellingly that the 1996 Constitution does have horizontal application.

\(^\text{18}\) See Havenga op cit note 16 at 276; Van Aswegen op cit note 16 at 52ff.

\(^\text{19}\) Policy considerations are applied in instances where the traditional area of application of an established rule has to be expanded to meet social, scientific or technological circumstances, or where settled rules have to be altered to accommodate novel factual circumstances. In addition, they apply where legal rules expressly or by implication incorporate them in their application. See generally Van Aswegen op cit note 16 at 59ff; Annel van Aswegen ‘Policy Considerations in the Law of Delict’ (1993) 56 THRHR 171 at 173–174 and 180–188; Payen Components SA Ltd v Bovic Gaskets CC & Others 1994 (2) SA 464 (W) at 474–476.

\(^\text{20}\) Section 24 of the Constitution.

\(^\text{21}\) Section 25. It is submitted that the provisions in the Companies Act which allow a court to facilitate reconstruction or amalgamation (see s 313) will have to be revised.

responsibility refers to behaviour that involves voluntarily sacrificing profits, either by incurring additional costs in the course of the company's production processes, or by making transfers to non-shareholder groups out of the surpluses thereby generated, in the belief that such behaviour will have consequences superior to those flowing from a policy of pure profit maximisation. Whether corporate decision-making should be guided purely by considerations of profit or should take account of the interests of third parties and social welfare more generally, has been seriously argued at least since the Berle-Dodd debate in America in 1932. Increasingly, the suggestion is that modern company directors should be entitled, and perhaps even obliged, to take the wider public interest into account. It is said that in an increasingly complex society the aim of the board of directors can no longer be the simple one of immediate profitability, and that a board ought to reconcile several different interests of which profit is the main, but cannot be the only one.

An obvious area of potential conflict between profitmaking for the benefit of the shareholders and fulfillment of other, more charitable, purposes, is that of corporate donations. Two American decisions illustrate the shift in attitude towards corporate gifts in the United States of America. In 1919, in *Dodge v Ford Motor Co*, the management of a very successful American car manufacturing company thought that the shareholders had already received adequate dividends and wished to utilise the surplus funds to pursue a course of conduct which would benefit the general public. The idea was for the company to cut prices and thereby to make cars more readily available to the general public, thereby stimulating the market and securing the jobs of company employees. However, the shareholders succeeded in forcing a dividend from the company. The Court considered it was not within the lawful powers of a board of directors to shape and conduct the affairs of a corporation for the merely incidental benefit of the shareholders and for the primary purpose of benefiting others. By contrast, some years later, a gift to Princeton University was upheld in *AP Smith Manufacturing Co v*
Barlow.\textsuperscript{27} The Court held that modern conditions require that corporations acknowledge and discharge social as well as private responsibilities as members of the communities in which they operate. It commended the company's long-visioned action in recognising and voluntarily discharging its high obligations as a constituent of our modern social structure.\textsuperscript{28} American courts now generally acknowledge that directors may consider the national economic interest, as well as environmental and educational concerns.\textsuperscript{29}

In early English case law the courts' rejections of corporate gifts were based on the doctrine of ultra vires.\textsuperscript{30} Transactions entered into by a company which did not directly further its objectives were considered beyond the capacity of the company and were therefore void. But in England too the emphasis quickly shifted towards acceptance of a rather remote potential benefit to the company as sufficient to justify a donation.\textsuperscript{31} No problems as to capacity or power to make donations or to pay gratuities should ordinarily arise under South African law.\textsuperscript{32} Sections 33 and 34 of the Companies Act provide for a company to have ancillary objects and plenary powers to its main object or objects.\textsuperscript{33} The powers

\textsuperscript{27} 39 ALR 2d 1179 (NJ 1953).

\textsuperscript{28} See at 1192.

\textsuperscript{29} See AR Coleman 'Duties of Directors of Corporate Trustees to Beneficiaries' 1984 Companies and Securities LJ 147; Conard op cit note 26 at 941; Dawson op cit note 25 at 74–75 and authorities cited there; Michael K Tarver 'The Arrogance of Corporate Power: A Study of the Evolution of the Fiduciary Duty Owed by Management to the Corporation or Its Shareholders' (1967) 42 Tulane LR 155; The Sylvia Martin Foundation Inc v John E Swearingen 260 F Supp 231 (SDNY 1966) (national economic interest); Shlensky v Wrigley 237 NE 2d 766 (Ill App 1968) (environmental interests); Theodora Holding Corporation v Henderson 257 A 2d 398 (Del 1969) (educational interests). The proposals of the American Law Institute's Corporate Governance Project confirm this viewpoint in recognising that a company 'may devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes' regardless of corporate profit or shareholder gain. See American Law Institute Principles of Corporate Governance: Analysis and Recommendations: Proposed Final Draft (1992) par 2.01 and accompanying commentary. The limit set on corporate philanthropy is apparently determined by a standard of reasonableness: see Faith Stevelman Kahn 'Pandora's Box: Managerial Discretion and the Problem of Corporate Philanthropy' (1997) 44 University of California at Los Angeles LR 579 at 606.

\textsuperscript{30} See Hutton v West Cork Railway Company (1883) 23 ChD 654; Tomkinson v South-Eastern Railway Company (1887) 35 ChD 675; In re Lee, Behrens & Company, Limited [1932] 2 Ch 46; Parke v Daily News Ltd [1962] Ch 927. See also In re W & M Roith Ltd [1967] 1 WLR 432 where the Court held that the payment of a pension to a director's widow in terms of his service agreement, had not been for the benefit of and to promote the prosperity of the company and was thus ultra vires the company. On the distinguishing features between Lee and Roith, see Harry Silberberg 'Gratuitous Payments for the Benefit of a Company' 1968 J of Business Law 213.


\textsuperscript{32} Before the Companies Act 1973 came into operation, such a donation was considered ultra vires and void: see Amalgamated Society of Woodworkers of SA & Another v Die 1963 Amalgamated Society 1967 (1) SA 586 (T) at 595C.

\textsuperscript{33} Section 33 provides that a company shall have the capacity determined by the main object stated in its memorandum and that there shall be included in its capacity unlimited objects ancillary to the said main object, except such specific ancillary objects as are expressly excluded in its memorandum. Section 34 states that, subject to limitations imposed by the Act, every company shall have plenary powers, including the common powers stated in Schedule 2 to the Act, to enable it to realise its main and ancillary objects, except such specific powers as are expressly excluded or qualified in its memorandum. The common powers in Schedule 2 include the powers '(o) to make donations' and '(r) to pay gratuities and pensions and establish pension schemes, profit-sharing plans and other incentive schemes in respect of its directors, officers and employees'.
may, of course, be specifically excluded, but s 36 restricts the capacity to set aside donations or charitable gifts that have already been made. The section provides that although an act of a company may be ultra vires, it is not void by reason only of that fact. However, the directors may still incur personal liability for any loss or damage the company may suffer as a result of an ultra vires act. Even in an essentially commercial company, I consider it unlikely that modern directors will necessarily be considered in breach of their fiduciary duty for making corporate gifts. The circumstances at the time when the particular gift was made naturally remain an important consideration in the assessment, and the maximisation of shareholder wealth should remain the directors’ overriding duty. Of course corporate social responsibility extends beyond corporate gifts. Product safety, environmental protection, the removal of gender and racial discrimination, the fair treatment of suppliers, and the maintenance of employees’ health and safety are other modern corporate social concerns. The Constitution addresses some of them directly. The equality clause contained in s 9 states that no person may unfairly discriminate directly or indirectly against anyone on one or more grounds, including race, gender, sex, pregnancy, marital status, ethnic or social origin, colour, sexual orientation, age, disability, religion, conscience, belief, culture, language and birth. And environmental concerns are regulated by s 24 which provides that everyone has the right to an environment that is not harmful to their health or well-being; and to have the environment protected for the benefit of present and future generations, through reasonable legislative and other measures that prevent pollution and ecological degradation, promote conservation, and secure ecologically sustainable development and use of natural resources while promoting justifiable economic and social development. Directors who disregard these provisions may, in addition to possible sanctions

34 Section 36 provides that no act of a company shall be void by reason only of the fact that the company was without capacity or power so to act, or because the directors had no authority to perform that act on behalf of the company for that reason.
35 This is apparent from the proviso in s 36 that ‘except as between the company and its members and its directors, or as between its members and its directors’ neither the company nor any other person may in any legal proceedings assert or rely upon any such lack of capacity or power. See also MS Blackman ‘The Capacity, Powers and Purposes of Companies: The Commission and the New Companies Act’ (1975) 8 Comparative and International LJ of South Africa 1 at 39; MS Blackman ‘Blackman’s Duty to Exercise Their Powers for an Authorised Business Purpose’ (1990) 2 SA Merc LJ 1 at 9; RC Beuthin & SM Luiz Beuthin’s Basic Company Law 2 ed (1992) at 89; Cilliers et al op cit note 1 at 181; Du Plessis Groenblad op cit note 8 at 12; MG Fredman ‘A Note on Section 36 of the Companies Act’ (1982) 99 SALJ 283 at 286ff; Hahlo op cit note 5 at 102–103; Henochsberg on the Companies Act by Phillip M Meskin (ed) 5 ed (1994) at 64–68; SJ Naudé ‘Company Contracts: The Effect of Section 36 of the New Act’ (1974) 91 SALJ 315.
36 See also Parkinson op cit note 23 at 279.
38 See also s 8 of Act 200 of 1993 which contains similar provisions. See in general Catherine Albelyn & Janet Kentridge ‘Introducing the Right to Equality in the Interim Constitution’ (1994) 10 South African J on Human Rights 149. On the effect of the equality provisions on insurance law, see Havenga op cit note 16 at 277 et seq.
imposed by specific statutes, or other common-law liability, be held to be in breach of their fiduciary duties to the company. It may also be expected that public policy will demand broader consideration of those concerns which are not directly addressed in the Constitution.

### 3 The Beneficiary of the Fiduciary Obligation

Acceptance of the fact that a company’s managers should consider various concerns leads to the second matter that I wish to address, namely the beneficiary of a director’s fiduciary obligation.

The entity to which the directors owe fiduciary duties is commonly explained as ‘the company as a whole’, a phrase described by Sealy as ‘of notoriously elusive meaning’. The phrase ‘the company as a whole’ has in the past been interpreted as the shareholders collectively, ‘all the shareholders, present and future’, and the company as a separate legal entity.

The view of profit-sacrificing social responsibility to which I referred above, forms the essence of the stakeholder theory of corporate governance and indicates a deviation from identifying the interests of the company with the financial interests of its shareholders towards viewing the company as a separate entity in which many conflicting interests, such as those of its shareholders, creditors, employees, as well as environmental and consumer concerns, should be accommodated. A growing body of cases suggests that not only should the interests of one or more of the stakeholders be considered, but that the stakeholders should, at least in certain circumstances, be direct beneficiaries of a director’s fiduciary duty. This would have far-reaching consequences especially with regard to ratification of breaches of the duty and in respect of its enforcement. New Zealand courts have considered the family character of the company, the directors’ positions in the company,

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41 See LS Sealy ‘“Bona Fides” and “Proper Purposes” in Corporate Decisions’ (1989) Monash University LR 265 at 269. Sealy contends that the attempt by modern commentators to make it mean all things to all men by adding gloss after gloss — shareholders present and future, employees and creditors — results in an emerging ill-focused conglomerate. See also DD Prentice ‘Creditor’s Interests and Directors’ Duties’ (1990) 10 Oxford J of Legal Studies 265 at 273, who indicates that the concept of ‘interests of the company’ is often indeterminate and sometimes arguably incoherent.
42 See OJS Fourie ‘Die Plig van Direkteure Teenoor Maatskappyskuldeisers’ (1992) 4 SA Merc LJ 25 at 26–27 and authorities cited there. In Gaiman v National Association for Mental Health [1971] Ch 317 at 330 Megarry J suggested that ‘the interests of some particular section or sections of the company cannot be equated with those of the company, and I would accept the interests of the company and future members of the company, as a whole, as being a helpful expression of a human equivalent’.
their high degree of inside knowledge and the way they went about a
take-over as indicative of the existence of a director-shareholder fiduciary
relationship.\textsuperscript{44} Australian courts too have indicated their willingness to
recognise a fiduciary relationship between directors and individual
shareholders in appropriate cases.\textsuperscript{45} And fiduciary duties between
directors and creditors of the company have been recognised in several
jurisdictions, again where special circumstances existed such as the
insolvency or near insolvency of the companies involved.\textsuperscript{46} In the
Australian decision in \textit{Jeffree v National Companies & Securities
Commission}\textsuperscript{47} it was stated unequivocally that the directors owe a
fiduciary duty to company creditors. Jeffree was a director of Wanup, a
trustee company of the Jeffree Family Trust. The trust carried on a
business constructing swimming pools. Arbitration proceedings were
instituted by one Leighton for defects in the construction of a swimming
pool. Wanup, acting in accordance with legal advice and apparently with
the unanimous assent of its shareholders, paid its creditors and sold its
assets at full value to a new legal entity called Cassidy. Cassidy had been
incorporated with the same directors, shareholders and trustee establish-
ment, and effectively took over the running of the business. When
Leighton eventually obtained a judgment for the amount of the
arbitration award, Wanup was no more than a dormant shell and its
only asset was the debt due from Jeffree's new company. The Western
Australian Supreme Court held that in authorising the transfer of
Wanup's assets to Cassidy in order to defeat the arbitration claim, Jeffree
had improperly used his position to gain an advantage for himself.\textsuperscript{48} In its
explanation of why the purpose of the transfer was considered improper,
the Court stated that the directors owed a duty to the company's
creditors, present and future, to keep the company's property inviolate
and available for the repayment of its debts.\textsuperscript{49} Since the finding of an
improper purpose does not require a positive duty to act in the interests

\textsuperscript{44} See Coleman \textit{v Myers} [1977] 2 NZLR 297 (CA) at 324.
\textsuperscript{46} See Jeffrey Lawrence 'The Coleman \textit{v Myers} Fiduciary Relationship: An Australian
Resurgence?' (1996) 14 \textit{Company and Securities LJ} 428 for a discussion of recent Australian
decisions on this point.
\textsuperscript{47} (1989) 15 ACLR 217, 7 ACLC 556. For discussions of this case, see R Baxt 'A Senior
Australian Court Gives the "Thumbs-Up" to the Winkworth Principle — Directors Owe a Duty
to Creditors Both Present and Future' (1989) \textit{Company & Securities LJ} 344; R Baxt 'Getting Your
Directors' Duties (or Interests) Right — The Western Australia Full Court Endorses a Radical
English Decision that Directors Owe Duties to Future Creditors' (1989) \textit{Australian Business LR
\textsuperscript{48} Action had been instituted in terms of s 229(4) of the Companys (Western Australia) Code,
which provides: 'An officer or employee of a corporation shall not make improper use of his
position as such to gain, directly or indirectly, an advantage for himself or for any other person or
to cause detriment to the corporation.' The Court unanimously held that the directors had acted
for the impermissible purpose of defeating the interests of contingent creditors.
\textsuperscript{49} (1989) 15 ACLR 217 at 221 per Wallace J and at 227 per Brinsden J.
of the company creditors, it may be argued that the Court’s ruling in this regard did not affect the outcome of the case.\textsuperscript{50}

However, case law does not generally go as far as to suggest that a fiduciary duty always exists between the directors and these stakeholders. And in some jurisdictions, the statutes confirm the duty as existing between the directors and the corporation. In Canada, eight of the ten provincial legislatures oblige directors to exercise their powers in the best interests of the corporation.\textsuperscript{51} This is also the case under the federal Canada Business Corporations Act of 1985.\textsuperscript{52} The New Zealand Companies Act of 1993 provides that the fundamental duty of every director, when exercising powers or performing duties as a director, is to act in good faith and in a manner that he or she believes on reasonable grounds is in the best interests of the company.\textsuperscript{53} In England, the Companies Act of 1985 provides that directors shall have regard to the interests of the company’s employees and members\textsuperscript{54} but stresses that the duty is owed to the company and is enforceable in the same way as any other fiduciary duty owed to a company by its directors.\textsuperscript{55} Consequently, it is only if a company’s employees are also shareholders that they can, in their capacity as shareholders, enforce the director’s obligation to have regard to the company’s employees.\textsuperscript{56}

I have several concerns about the extension of the fiduciary relationship beyond the company as beneficiary.\textsuperscript{57} In the first instance, a fiduciary relationship is an ‘illusory concept’ incapable of universal definition.\textsuperscript{58} The existence and extent of such a relationship is determined by the facts and circumstances involved.\textsuperscript{59} Nevertheless, it seems that at least an undertaking, either expressly or by implication, by someone to act in relation to a matter in the interests of another in a manner which is understood by both parties and where the interests of the other party may

\textsuperscript{50} See also Worthington op cit note 11 at 136.
\textsuperscript{51} See Bruce Welling Corporate Law in Canada: The Governing Principles 2 ed (1991) at 437.
\textsuperscript{52} RSC 1985 c C-44, s 122(1)(a).
\textsuperscript{53} Section 101.
\textsuperscript{54} See Bruce Welling Corporate Law in Canada: The Governing Principles 2 ed (1991) at 437.
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\textsuperscript{57} This is generally regarded as a shortcoming of the statutory attempt to protect employees in English law: see Robert R Pennington Directors’ Personal Liability (1987) at 66. See also Allan Lowrie Mackenzie ‘The Employee and the Company Director’ (1982) 132 New LJ 688 who opines (at 690) that the duty should be owed to and enforceable by employees. See also David Millman ‘From Servant to Shareholder: Protecting the Employee Interest in Company Law’ in: David Feldman & Frank Metzel (eds) Corporate and Commercial Law: Modern Developments (1996) at 159 where the author points out that a possibly unforeseen consequence of s 309 is that it is used as a defence by company directors when their exercise of managerial discretion is questioned.
\textsuperscript{58} In this regard, see Havenga op cit note 46 at 48–53.
\textsuperscript{59} Gill op cit note 6 explains at 105 that while its existence is not doubted, the fiduciary relationship is not susceptible to precise definition, nor would it seem is its presence in any given situation guided by any discernible principle.
\textsuperscript{60} See also Havenga op cit note 46 at 8–11 and authorities cited there.
be affected, is required. The nature and circumstances giving rise to the undertaking should be such that loyalty and good faith are intrinsic elements of the consequent duty. It cannot be stated as a categorical rule that these requirements exist in the relationships between directors and the various interest groups mentioned.

Also, an extension of the duty owed by directors to include the interests of any other interest group would place this group in a superior position to other stakeholders, resulting in unequal treatment and, possibly, the loss of effective control. In the absence of substantive principles as to how the conflicting interests of the various stakeholders are to be resolved, or at least of some system of ranking, management will not be able to manage, or will do so somewhat randomly. And in many of the cases where it was attempted to identify duties to particular interest groups, the same result could have been achieved by application of established company law principles. In the Jeffree case discussed earlier, the Court could have found that Jeffree had exercised his powers for the improper purpose of defeating a creditor or of obtaining a personal benefit, or that he had breached his fiduciary duty to the company either by not acting in good faith in its interests, or by misusing his position for personal gain or by allowing his personal interests to conflict with his duty, or possibly that he had acted fraudulently. Although the results in these cases have on the whole been satisfactory, the danger exists that broader consequences than those foreseen in the particular circumstances, may ensue. This in turn may lead to legal uncertainty.

The fiduciary obligation is enforceable against a director by the company, or by a member making use of a derivative action. Should a

60 Gautreau op cit note 6 at 7. See also Gerard McCormack 'Fiduciaries in a Changing Commercial Climate' (1997) 18 Company Lawyer 38 at 39 and the authorities referred to in note 59 above.

61 See also Alcock op cit note 43 at 179; JE Parkinson 'The Contractual Theory of the Company and the Protection of Non-shareholder Interests' in: David Feldman & Frank Meisel (eds) Corporate and Commercial Law: Modern Developments (1996) at 142. As was mentioned above (see the text at n56 and n56 itself), s 309 of the English Companies Act 1985 does not provide any guidance on how the interests of the members and employees should be reconciled. The matter presumably rests within the business judgment of the directors: see Palmer's Company Law op cit note 11 at 8106.

62 See supra note 47 and also Havenga op cit note 46 at 39; Worthington op cit note 11 at 136.

63 The rule in Foss v Harbottle (1843) 2 Hare 461, 67 ER 189 provides that it is the company that must institute action when it has suffered a wrong. Should the company fail to do so a member may, in certain instances, institute action on behalf of the company. Even so, a member cannot act if the wrong concerned is one which a simple majority could condone or ratify. See generally Farrar op cit note 9 at 449; Gower op cit note 9 at 645ff; Naudé Maatskappydirekteur op cit note 5 at 168ff; Van Rooyen op cit note 11 at 39 and 102; KW Wedderburn 'Shareholders' Rights and the Rule in Foss v Harbottle' 1957 Cambridge LJ 194; KW Wedderburn 'Shareholders' Rights and the Rule in Foss v Harbottle' 1958 Cambridge LJ 93. On the rule in Foss v Harbottle and its application in South African law generally, see Cilliers et al op cit note 1 at 289ff; Hashio op cit note 5 at 507ff and authorities cited there; MacDougall v Gardiner (1875) 1 ChD 13; Shuttleworth v Cox Bros & Co (Maidenhead) Ltd [1927] 2 KB 9 (CA); Yende v Orlando Coal Distributors (Pty) Ltd 1961 (3) SA 314 (W); Sammel & Others v President Brand Gold Mining Co Ltd 1969 (3) SA 629 (A); Makhuva & Others v Lukoto Bus Service (Pty) Ltd & Others 1987 (3) SA 376 (VSC) at 394A; James North (Zimbabwe) (Pty) Ltd & Others v Mattinson 1990 (2) SA 228 (ZH) at 234E–F; McIlland v Hulett (1992) 1 SA 456 (D), discussed by BA van der Merwe 'Die Beskerming van Minderheidsaandeelhouders: Die Toepassingsveld van die Reel in Foss v Harbottle Uitgebrei?' (1993) 5 SA Merc LJ 216.
fiduciary duty exist between directors and any specific stakeholder, a member of that group should likewise be able to enforce it. Proponents of the stakeholder theory have not yet addressed this matter adequately.\footnote{64} And issues such as the restrictions on shareholders’ power to approve beforehand or to ratify breaches of directors’ duties remain unresolved.\footnote{65} Moreover, where creditors are involved, the fact that they charge interest for the services they render has not been taken into account. Creditors should not complain that insolvency has caused them loss because they have contracted to bear that risk, and have built compensation for bearing it into the cost of the credit.\footnote{66} It is, in any event, debatable whether, in view of the existing authorities favouring the company as beneficiary of directors’ duties, courts of law are the proper forum for wider recognition. I suggest that, in the interest of legal certainty, such wider recognition, if deemed desirable, should be provided for in legislation.

Directors’ conduct should be evaluated according to the way in which the interests of the company were served. Obviously this evaluation cannot take place in isolation and various factors, depending on the circumstances of each case, merit consideration. Amongst these one may well find the interests of other groups. I submit that legislation specifically aimed at a particular stakeholder achieves better protection than an extension of the fiduciary obligation would. The statutory measures aimed at the protection of shareholders\footnote{67} with regard to insider trading serve as an example.\footnote{68} And s 424 of our Companies Act gives substantial protection to company creditors. This section provides that a court may, on the application of certain persons including any creditor, impose personal liability on any person who was knowingly a party to the carrying on of the business of a company fraudulently, or in a reckless manner, or with intent to defraud creditors of the company or any other person.\footnote{69} Several other sections in the Act afford at least some measure of protection to creditors.\footnote{70}

\footnote{64} See Du Plessis op cit note 8 at 126; JJ du Plessis ‘Direkteure se Pligte teenoor Partye Anders as die Maatskappy’ 1993 De Jure 378 at 388–389; Worthington op cit note 11 at 151.
\footnote{65} See generally Havenga op cit note 46 at 394ff and authorities cited there.
\footnote{67} The generally accepted view remains that directors do not owe fiduciary duties to individual shareholders: Cilliers et al op cit note 1 at 144; Du Plessis ‘Pligte’ op cit note 64 at 378–379 and authorities cited in n4; Farrar op cit note 9 at 380; Havenga op cit note 46 at 27ff; Edward Jacobs ‘Duties to Creditors’ (1988) 7 Litigation 310; Gower op cit note 9 at 551; Palmer op cit note 11 at 934; Razen Sappideen ‘Fiduciary Obligations to Corporate Creditors’ 1991 J of Business Law 365 at 386; Welling op cit note 51 at 387; Percival v Wright [1902] 2 Ch 421.
\footnote{69} On this section, see the authorities cited in Havenga op cit note 46 at 33 n45.
\footnote{70} See e g ss 37 and 226 in respect of loans made and security provided by companies or directors and officers, s 38 which prohibits the giving of financial assistance by a company for the
Statutory protection of company stakeholders need not be contained in the Companies Act. Employee interests in management decisionmaking is predominantly regulated by labour law. A novel mechanism in this regard was introduced by the Labour Relations Act 66 of 1995 which came into operation recently. The Act permits the establishment of workplace forums, thereby elevating worker participation to a principle of national economic policy enshrined in a statutory framework, without limiting the scope for ad hoc management-labour arrangements at plant level. A workplace forum may be established in any workplace in which an employer has more than one hundred employees. The intended purpose for the establishment of these forums is the promotion of the interests of all employees in the workplace, whether or not they are trade union members, through compulsory consultation and joint decision-making. If a workplace forum has been established, the Act obliges an employer to consult with it about proposals to effect certain changes in the workplace, unless the matters for consultation are regulated by a collective agreement with the representative trade union. These changes include restructuring of the workplace, plant closures, mergers and transfers of ownership in as far as they would impact on the interests of the employees, dismissals for operational reasons, and product development plans. If the employer and the workplace forum cannot come to an agreement, the employer must invoke any agreed procedure to resolve any differences before the employer’s proposal may be implemented. Other measures designed to protect employees, such as employee representation within a dual board system have been received with mixed acclaim in other jurisdictions and there is considerable debate about the desirability of their implementation in our system. Although

purchase of its own shares or the shares of its holding company, ss 83 and 84 in respect of the reduction of capital, s 219 with regard to the disqualification of directors and s 423 which enables the court to order the restoration of money or property of or compensation to the company where it appears that any person who has taken part in the formartion or promotion of the company or any director or officer has misapplied, retained or become liable or accountable for such money or property.

It is likely that securities regulation will be removed from the Companies Act as has been the case in other jurisdictions. And the provisions under English law similar to those of s 424 of our Companies Act are found in s 214 of the Insolvency Act 1986 (c 45).

This Act marks a major change in South Africa’s statutory industrial relations system. See D du Toit, D Woolfrey, J Murphy, S Godfrey, D Bosch & S Christie The Labour Relations Act of 1995 (1996) at 3 who cogently summarise its objectives: ‘Following the transition to political democracy, the Act encapsulates the new government’s aims to reconstruct and democratise the economy and society in the labour relations arena. It therefore introduces new institutions that are intended to give employers and workers an opportunity to break with the intense adversarialism that has characterised their relations in the past.’


See Du Toit op cit note 72 at 229.

Section 80(1).

Section 79.

Section 84(1).

Section 85(4).

On these aspects generally, see JJ du Plessis ‘Corporate Governance: Reflections on the German Two-tier Board System’ (1996) 1 J of South African Law 20; JV du Plessis ‘Werkers-
some reservations have been expressed about the need for workplace forums,\textsuperscript{81} the attempt at protection of employees' interests in the Labour Relations Act must be welcomed. However, the present regulation has the anomalous effect that should the company suffer damage as a result of a decision taken in the employees' interests at a workplace forum, the directors may be liable to the company for breaching their fiduciary duty.\textsuperscript{82} I submit that this matter will have to be addressed.\textsuperscript{83}

It is generally recognised that our Companies Act is in need of comprehensive review. For the sake of legal certainty and in view of the problems mentioned above, I am of the opinion that our company law would benefit from a general statement of directors' fiduciary duties in the Act. This statement should aim at informing and not be designed to replace the existing common law. It should confirm that fiduciary obligations are owed to the company, whilst permitting consideration of other stakeholders' interests. Nominee directors, who are appointed to represent the interests of a specific person or class of persons, face a fundamental conflict. They owe a duty to act in the best interests of the company to which they are appointed, but at the same time are expected by their appointor to protect the interests of the appointor. Arguably the nominee director is unable always to act in the best interests of the company in those circumstances. I suggest that they should be permitted to pay specific attention to the interests of the person or class who appointed them, subject to the proviso that the interests of the company prevail. They will therefore be absolved from suggested breach of duty to the company if they acted in furtherance of the interests of their appointors, provided that their conduct accords with a genuine belief that the interests of the company were being advanced.

4 Conclusion

In conclusion, directors should be accountable for the way in which they exercise their powers. The recognition and enforcement of a strict fiduciary relationship between director and company is potentially an important means of exercising control over company management. But

\textsuperscript{81} See Piet Delport 'Korporatiewe Reg en Werkplekforums' (1995) 2 De Jure 409 at 417–418; Employers fear a loss of their managerial prerogative, resulting, eventually, in a total inability to manage the undertaking as they see fit. The main objection from trade unions appears to be that their representative role on the factory floor may be diminished: see Carl Mischke 'The Shape of Things to Come — The New Labour Relations Act' (1995) 3 Juta's Business Law 150 at 151.

\textsuperscript{82} See also De Toit et al op cit note 72 at 229–230.

\textsuperscript{83} In this regard, see also s 210 of the Labour Relations Act which provides that in any conflict arising between the Labour Relations Act and the provisions of any other law the Constitution or any Act expressly amending the Labour Relations Act, the provisions of the Labour Relations Act will prevail.
effective enforcement is only possible if both content and extent of the common-law obligation are ascertainable. I therefore recommend that the duty be restated in general terms in the Companies Act and that the company laws of Canada, Australia and New Zealand provide useful guidelines in this regard. I remain of the opinion that directors’ fiduciary duties are owed to the company as a whole, and not to individual shareholders, creditors or other stakeholders. The provisions of the Labour Relations Act necessitate specific regulation of the accountability of directors for decisions taken at a workplace forum. Stakeholders’ interests may clearly not be disregarded. The Bill of Rights contained in the South African Constitution will inevitably influence the interpretation of any open-ended standard and must affect the determination of good faith in the assessment of a director’s compliance with her fiduciary duty. Public policy will probably attach greater importance to wider social responsibilities and concern for the stakeholders’ interests. Hopefully the courts will have the opportunity to indicate their approach in this regard.

INSURANCE FRAUD

‘In 1993, New Jersey’s insurance fraud division staged a series of bus accidents in which the only passengers were state fraud investigators. The sting operation implicated more than 100 persons who claimed injuries after either jumping on the buses immediately after the accident or filing a claim after driving by the scene.

Although alarming, this is not an isolated incident of insurance fraud; it repeats itself every day in various forms in cities, large and small, across the nation. In fact, fraud has been a plague on the institution of insurance from the time people first began pooling their resources to minimise the risk of individual financial losses.

Nevertheless, criminal prosecution of insurance fraud is a low priority with law enforcement and prosecutors. As one prosecutor put it, insurance fraud is simply one thief stealing from another.’