CONTESTING THE REMOVAL OF A DIRECTOR BY THE BOARD OF DIRECTORS UNDER THE COMPANIES ACT

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Section 71(3) of the Companies Act 71 of 2008 has introduced a novel power into our company law, which permits the board of directors of a company under certain circumstances to remove a director from office. While there may be merits in vesting a company's board of directors with this power, concerns arise whether the fear of removal from office would stifle the actions of a director in managing the company's affairs, whether the power would be abused, and whether the board of directors could act with ulterior motives in removing a diligent director from office. In Pretorius v PB Meat (Pty) Ltd *[2013] ZAWCHC 89, the Western Cape High Court shed some light on the interpretation of s 71(4) of the Companies Act 71 of 2008 and on the power of a director to contest his removal from office. Although the Companies Act 71 of 2008 makes some provision for a director to contest his removal from office by the board of directors, a director who has been unfairly removed from office by the board of directors will nevertheless face certain difficulties. In light of these difficulties and as a result of the* Pretorius *decision, it is important to guard against the potential for abuse of this new power by boards of directors.*

I INTRODUCTION

The Companies Act 71 of 2008 ('the Companies Act') has introduced a novel provision into South African company law which permits the board of directors of a company under certain circumstances to remove a director from office. Previously, under s 220 of the Companies Act 61 of 1973 ('the Companies Act of 1973'), only the shareholders were statutorily empowered to remove a director from the board of directors. This new provision in the Companies Act, which is contained in s 71(3), vests the board of directors of a company with powers that they did not possess under the previous company-law regime.

While there may be merits in vesting a company's board of directors with the power to remove one of their own from office, concerns arise whether the fear of being removed by the board of directors would stifle or inhibit the actions of a director in managing the affairs of the company. A further concern is whether this new power would be abused by the board of directors, and whether the board of directors would act with ulterior motives in removing a vigilant or diligent director from office. Although the Companies Act does contain certain provisions upon which a director may rely to contest his impending removal from office or to contest his removal after it has occurred, the question arises whether these provisions are

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sufficiently effective to protect a director who has been unfairly removed from office in terms of s 71(3).

In the recent case of *Pretorius v PB Meat (Pty) Ltd*[1] ('*Pretorius*'), Cloete J of the Western Cape High Court handed down the first judgment on s 71 of the Companies Act. The case dealt with the proposed removal of two directors by the board of directors, in circumstances where the directors concerned had contested their removal. In the course of its judgment, the court shed some light on the power of a director to contest his removal from the board of directors, and on the interpretation of s 71(4) of the Companies Act.

This article begins in part II below with a brief examination of the procedure to remove a director by the board of directors. Then, part III considers the impact of the power of removal on the dynamics and internal workings of the board of directors. Thereafter, part IV examines the *Pretorius* judgment and the principles which emerge from it. Finally, part V looks at whether, and in light of the *Pretorius* judgment, directors are able effectively to contest their removal from the board of directors.

II THE PROCEDURE TO REMOVE A DIRECTOR

(a) Removal by the board of directors where a company has more than two directors

Under s 71(3) of the Companies Act, if a company has more than two directors, and a shareholder or director alleges that a director has become ineligible or disqualified in terms of s 69 of the Companies Act (other than on the grounds contemplated in s 69(8)*(a)*),[2] has become incapacitated to the extent that the director is unable to perform the functions of a director and is unlikely to regain that capacity within a reasonable time, or has neglected or been derelict in the performance of the functions of a director, the board (other than the director concerned) must determine the matter by resolution, and may remove such a director. The phrase in s 71(3), 'must determine the matter by resolution', means that if such an allegation has been made by a shareholder or director, the board of directors is obliged to determine the matter by resolution. However, s 71(3) goes on to say that the board 'may remove a director', meaning that the board of directors has a discretion whether or not to remove the director in question from office.

Before the board of directors considers a resolution to remove a director from office, the director concerned must be given notice of the board meeting, together with a copy of the proposed resolution. This must also include a statement setting out reasons with 'sufficient specificity' for the proposed resolution, to permit the director concerned reasonably to prepare

[1] [2013] ZAWCHC 89.

[2] In terms of s 69(8)*(a)* a person will be disqualified from being a director of a company if a court has prohibited that person from being a director, or has declared the person to be delinquent in terms of s 162 of the Companies Act or s 47 of the Close Corporations Act 69 of 1984.

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and present a response.[3] In addition, the director concerned must be given a reasonable opportunity to make a presentation, either in person or through a representative, before the resolution is put to the vote.[4]

In terms of s 71(5) of the Companies Act, if the board of directors has removed a director from office, the director concerned or a person who appointed that director in terms of the Memorandum of Incorporation as contemplated in s 66(4)*(a)*(i), if applicable, may apply to court within twenty business days to review the board's determination. Under s 71(6) of the Companies Act, if the board of directors has determined that a director is not ineligible, disqualified or incapacitated, or has not been negligent or derelict, any director who voted otherwise on the resolution, or any shareholder entitled to vote in the election of that director, may apply to court to review the board's determination.[5] In such a review, a court may either confirm the board's determination not to remove the director in question, or it may remove the director from office if it is satisfied that the director in question is indeed ineligible, disqualified, incapacitated or has been negligent or derelict.[6]

(b) Removal by the Companies Tribunal where a company has fewer than three directors

In a company with fewer than three directors, which would be a private company, the board of directors itself is not empowered to remove a director from its board.[7] Instead, a director or shareholder of the company may apply to the Companies Tribunal to determine the director's removal from office on the same grounds set out in s 71(3).[8] The procedures which apply to the removal of a director by the board of directors, as set out in s 71(4) and outlined above, would apply likewise to the determination of the matter by the Companies Tribunal.[9]

(c) Removal by the shareholders

The new Companies Act has retained the powers previously conferred on shareholders to remove a director. In terms of s 71(1) of the Companies Act, a director may be removed from the board of directors by means of an ordinary resolution passed by the shareholders in a shareholders' meeting, despite anything to the contrary in the company's Memorandum of Incorporation,

[3] Section 71(4)*(a)* of the Companies Act.

[4] Section 71(4)*(b)* of the Companies Act.

[5] Section 71(6)*(a)*.

[6] Section 71(6)*(b)*. Unless the court reverses the board's determination, the applicant in such a review application would be liable to compensate the company and any other party for the costs incurred in relation to the application (s 71(7)).

[7] Section 71(8)*(a)* of the Companies Act.

[8] See s 71(8)*(b)* of the Companies Act.

[9] Section 71(8)*(c)* of the Companies Act. See Farouk H I Cassim, Maleka Femida Cassim, Rehana Cassim et al *Contemporary Company Law* 2 ed (2012) 449–50 for a discussion of these procedures.

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or rules, or any agreement between the company and the director or any shareholders and a director. The removal of a director by the shareholders must follow a similar procedure to that followed when the board of directors removes a director.[10] A detailed discussion of the removal of a director by the shareholders of a company is beyond the scope of this article.[11] There are however two important differences between the removal of a director by the board of directors and by the shareholders. The first is that for the shareholders to remove a director from office, no grounds of removal are required, as is the case with the removal of a director by the board of directors. Accordingly, when the shareholders, or a majority of them, purport to remove a director from the board of directors, they are not required to provide the director concerned with a statement setting out the reasons for the proposed resolution, as is the case when the board of directors purports to remove a director. Secondly, a decision by the shareholders to remove a director from the board of directors is not subject to review by a court, as is the case with the removal of a director by the board of directors.

The question thus arises: why would the board of directors wish to remove a director from office instead of requesting or convincing the shareholders to do so, when it is less complicated for the shareholders to do so? There may be several reasons for this. For instance, removal by the board of directors may occur when the shareholders who wish to remove a director from office do not have sufficient voting power to remove the director in question. Another instance when the board of directors may remove a director is where the shareholders do not in fact wish to remove a particular director, or are not convinced by the reasons advanced by the board to remove the particular director. There may also be instances where the board of directors does not wish to disclose to the shareholders their suspicions of a misdemeanour or a transgression by a particular director. For instance, the board may suspect that one of the directors on the board has disclosed confidential information to a third party, or is involved in a conflict of interest situation, or is engaged in an ethically questionable activity that will be embarrassing to the company if publicly known, or would expose the company to potential legal action. While such issues ought to be taken to the shareholders, the board of directors may fear that if they disclose their suspicions to the shareholders, the shareholders would consider instituting legal action against them.[12] In such

[10] See s 71(2) of the Companies Act.

[11] See Caroline Ncube 'You're fired! The removal of directors under the Companies Act 71 of 2008' (2011) 128 *SALJ* 33; Cassim et al op cit note 9 at 441–3 and Farouk H I Cassim 'The division and balance of power between the board of directors and the shareholders: The removal of directors' (2013) 29 *Banking and Finance LR* 151.

[12] See James McConvill 'Removal of directors of public companies takes centre stage in Australia' (2005) 191 *The Corporate Governance LR* 191 at 210 and Stephen Knight 'The removal of public company directors in Australia: Time for change?' (2007) 25 *Company and Securities LJ* 351 at 362.

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instances, the board of directors may choose to remove a director themselves, rather than requesting the shareholders to do so.

III THE IMPACT OF THE BOARD'S POWER OF REMOVAL ON THE DYNAMICS OF THE BOARD OF DIRECTORS

The pertinent question is whether this new power of the board of directors to remove one of their own from office impacts on the dynamics and internal workings of the board of directors. An immediate concern relates to whether the board of directors will use this power sensibly or with ulterior motives. For example, a performance assessment of a director must be done objectively and in a fair manner. However, it is possible that the board of directors may not objectively conduct the assessment of a particular director. A board, acting with ulterior motives, may declare that a director has failed to meet a broadly expressed or subjective performance standard[13] and, as a result, has been derelict in the performance of his functions, as contemplated in s 71(3)*(b)* of the Companies Act. This would constitute a ground for the removal of a director from office by the board of directors.

In order to guard against the danger of a performance assessment of a director being conducted subjectively or unfairly, directors must follow the recommendations of the King Report on Governance for South Africa 2009 ('King III Report'). The King III Report recommends that the evaluation of a director should be led by the chairperson through the nominations committee or by an independent service provider; a director's contribution to the board should be measured against his duties, and the evaluation must be approached in an open, constructive and non-confrontational manner.[14] Nevertheless, save for listed companies, these recommendations are persuasive and lack binding force. They would not necessarily prevent a director from being evaluated in a subjective or unfair manner that lacks transparency, particularly in the case of unlisted companies. On this note, David Gonski, the chairman of Coca-Cola Amatil Ltd, has asserted the following:

> 'Judgements on who is or who is not pulling their weight must be made by other board members; and I accept that some board members may not use that power objectively. That's human nature and we have to guard against that.'[15]

A further concern is whether this new power of the board of directors to remove a director would hinder free and open discussion and debate in board meetings. The fear or threat of removal could well have the effect of limiting dissent in the boardroom — a director may hesitate to express a dissenting

[13] See R P Austin & I M Ramsay *Ford's Principles of Corporations Law* 14 ed (2010) 263 para 7.240.

[14] Principle 2.22 of the King III Report and see also King III Report at 45 paras 116–18.

[15] Australian Institute of Company Directors 'David Gonski — The role of the chairman' available at *http://www.companydirectors.com.au/Director-Resource-Centre/Publications/Company-Director-magazine/2000-to–2009-back-editions/2005/March/David-Gonski-The-role-of-the-chairman-Cover-Story*, accessed on 11 August 2014.

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view on a particular matter.[16] More worryingly, if a director becomes aware of, or suspects wrongdoing by certain members of the board of directors, the threat of removal by fellow board members may result in the director failing to act or to investigate the wrongdoing. This would have negative consequences for shareholders and for the company itself.

Samuel Tak Lee v Chou Wen Hsien[17] provides a clear illustration of the danger of a pre-emptive removal of a director when he suspects wrongdoing by board members. In this case, the appellant, Lee, was a director on the board of directors of a company listed on the Hong Kong stock exchange. Lee had become suspicious about certain transactions concerning the company's subsidiary companies, including the sale of the company's shareholding in another company. He claimed that the company's shareholding in another company had been sold at an undervalue to a company, which he suspected was beneficially owned by the chairperson and managing director of the company, and by the chairperson's brother, who was the vice-chairman and deputy managing director of the company. To confirm his suspicions, Lee asked for access to various accounts, but his requests were denied. Lee then requested that a board meeting be convened so that he could discuss his concerns with the board of directors, but two days before the date of the meeting, he received a notice, signed by all of his co-directors, requesting him to resign immediately. The notice had been issued pursuant to article 73*(d)* of the company's constitution, which appeared under the heading 'Disqualification of directors' and stated that the office of a director shall be vacated if the director is asked, in writing, by all his co-directors to resign. Lee was consequently removed from the board of directors. In court, Lee contended that the notice given to him by the board of directors was invalid and of no effect and that he remained a director of the company.

In its judgment, the Privy Council ruled that the power given to directors to remove one of their members from the board of directors is a fiduciary power in the sense that each director concurring in the expulsion, must act in accordance with what he believes to be in the best interest of the company, and that this power must not be exercised with ulterior motives.[18] Nevertheless, the court ruled, it does not follow that the expulsion of a director from the board of directors would be void and of no effect merely because one or more of the directors had acted with an ulterior motive.[19] According to the Privy Council, to rule that bad faith on the part of any one director vitiates the removal of the director concerned would introduce a new source of uncertainty into the management of the company, which could bring the management of the company to a standstill because a company must be capable, at all times, of ascertaining precisely who its directors are.[20] The

[16] Knight op cit note 12 at 361; Cassim op cit note 11 at 162.
[17] [1984] 1 WLR 1202 (PC).
[18] Ibid at 1206.
[19] Ibid.
[20] Ibid at 1206–7.

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Privy Council thus held that Lee's removal from the board of directors was valid, even though in removing him, the board may have acted with ulterior motives and in breach of their fiduciary duties as directors.

Directors have a duty to observe the utmost good faith towards the company. In discharging this duty, each director is required to exercise an independent judgment, not fetter his discretion and take decisions according to the best interests of the company.[21] Accordingly, directors ought not to allow the fear of removal to limit dissent in the boardroom or to prevent them from expressing their views or investigating any suspected wrongdoing by the board of directors.[22] In most instances, the approval of a majority of the directors on the board of directors would be required to approve board decisions. In other words, not all decisions taken by the board of a company would require unanimity. Accordingly, a board of directors is not likely to remove a minority director when that minority director is not in a position to obstruct the workings of the board or to impede the will of the majority of the directors.[23] Nevertheless, a director who is about to expose a wrongdoing by the board of directors or is aware of misdemeanours by certain members of the board, may well be at risk of being removed by a board of directors with ulterior motives, as occurred in the case of *Samuel Tak Lee v Chou Wen Hsien*.[24]

So, if a director were removed in terms of s 71(3) of the Companies Act by a board of directors with ulterior motives, would he be able effectively to contest his removal? The Companies Act contains certain provisions on which a director may rely to contest his removal, but in light of the judgment in *Pretorius*, the question arises as to the effectiveness of these provisions. Before these issues are addressed, the *Pretorius* judgment is briefly examined.

IV THE *PRETORIUS* JUDGMENT

Pretorius dealt with the proposed removal of two directors by the board of directors under s 71(3) of the Companies Act. The first and second applicants were directors and employees of the company, PB Meat (Pty) Ltd ('the Company'). The applicants had resigned as employees of the Company but had refused to resign as directors, notwithstanding repeated requests to do so and a clause to the contrary in their respective service agreements. The clause in question required the applicants to resign as directors on termination of their employment and on the request of the Company. The applicants contended that this clause had been inserted in their service agreements as a result of a common mistake, but this was denied by the Company (the first respondent). As a consequence of the refusal of the applicants to resign as directors of the Company, the second respondent, a director on the board of

[21] See *Fisheries Development Corporation of SA Ltd v Jorgensen; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd* 1980 (4) SA 156 (W) at 163.

[22] Knight op cit note 12 at 361; Cassim op cit note 11 at 162.

[23] Knight ibid.

[24] Supra note 17.

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directors, had caused letters to be served upon the applicants to attend a meeting of the board of directors. This meeting had been convened to consider a proposed resolution to remove the applicants as directors on the basis that they had been derelict in the performance of their functions as directors.

A statement of reasons for the proposed removal of the applicants had been attached to the resolution provided to the applicants. Briefly, the reasons were that the applicants had unlawfully removed certain equipment owned by the Company from its premises and had installed such equipment at their own premises in order to use it for private purposes; that the applicants had unlawfully disposed of equipment owned by the Company and had retained the proceeds of such disposal instead of paying them to the Company; and that the applicants unlawfully had made a secret profit from the sale of certain products, which profit ought to have accrued to the Company.

After the receipt of the proposed resolution and statement of reasons, the attorney for the applicants delivered an eight page 'Request for Further Particulars and Specificity in terms of s 71(4)' of the Companies Act. The Company duly furnished a written response to the request for further particulars. The applicants, in turn, were of the view that these further particulars fell short of what was required reasonably to enable them to prepare a response for their presentation at the impending board meeting. Accordingly, their attorney delivered a 'Request for Access to Record of Private Body' in accordance with s 53(1) of the Promotion of Access to Information Act 2 of 2000 ('PAIA'). Amongst the documents requested, were certain financial statements, stock sheets, purchase invoices, value-added tax invoices and monthly management accounts of the Company.

The application for the above information was based on two grounds. First, the applicants contended that they were entitled to access to the documents in their capacities as directors of the Company, because as directors, they had a statutory obligation in terms of s 66(1) of the Companies Act to manage the business and affairs of the Company. The applicants maintained that if they were refused access to the requested information, they would be precluded effectively from fulfilling those obligations. Secondly, the applicants argued that in terms of s 50(1) of PAIA, they were entitled to the requested documents of the (private) Company because they had met the provision's specific requirements. The Company, by contrast, contended that the documents requested by the applicants were not necessary to protect the applicant's rights and that its refusal to provide them would not result in any prejudice to the applicants. The Company contended further that the documents contained sensitive commercial information which, in terms of s 68 of PAIA, is a ground for refusing access to the requested documents. The question to be decided by the Western Cape High Court was whether the documents requested by the applicants had to be produced by the Company in order to satisfy the 'sufficient specificity' requirement of s 71(4)*(a)* of the Companies Act.

The phrase 'sufficient specificity' has not been defined in the Companies Act and there was no equivalent provision in the Companies Act of 1973.

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Relying on the judgment of *Avril Elizabeth Home for the Mentally Handicapped v Commission for Conciliation, Mediation and Arbitration*[25] ('*Avril*'), the Western Cape High Court in *Pretorius* held that the phrase 'sufficient specificity' meant 'sufficiently detailed reasons to mount a response'[26] to the case for the proposed removal. The court stated that it is inherent in this formulation that each case ultimately must depend upon its own particular facts.[27]

The court rejected the first ground relied upon by the applicants. Cloete J found, on the applicants' own version, that they had not required the documents in order to manage the business and affairs of the Company. Rather, they had wished to have sight of the documents for the purpose of preparing and presenting a response to the allegations made against them.[28] In other words, the court found that the applicants' sole purpose in wanting access to the documents was not to protect the Company but to protect themselves as individual directors and to safeguard themselves against possible removal from the board of directors.[29] The court held further that the applicants, in their capacities as directors of the Company, were not entitled as of right, to access to the documents which they had requested.[30]

In regard to the second ground relied upon by the applicants, namely that they were entitled to the documents they had requested in terms of s 50(1) of PAIA on the basis that such documents were relevant to disprove the allegations made against them, the court examined the specific requirements that had to be complied with. Here, the court held that the applicants had not satisfied these requirements. In particular, the court was not satisfied that the documents required by the applicants would assist them in exercising or protecting their rights as envisaged by s 50 of PAIA. Crucial to the court's finding was the fact that the allegations made in the Company's statement of reasons for the applicants' removal were quite simple, and that the further particulars provided by the Company indicated that the allegations made against the applicants were comprised predominantly of eyewitness testimony.[31] In other words, there was no suggestion by the Company that the applicants were 'guilty of complex commercial fraud'.[32] The court stated that had that been the case, the position might well have been different.[33]

So, in light of the fact that the allegations made against the applicants had been simple and uncomplicated, the court held that access to the financial and commercial records of the Company, as sought by the applicants, would

[25] [2006] 9 BLLR 833 (LC). This is a decision of the Labour Court, which dealt with the concept of procedural fairness in the pre-dismissal procedure under the Labour Relations Act 66 of 1995 ('the LRA')

[26] Supra note 1 para 10.

[27] Ibid.

[28] Ibid para 23.

[29] Ibid paras 23 and 27.

[30] Ibid para 28.

[31] Ibid para 44.

[32] Ibid.

[33] Ibid.

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not assist them in any meaningful way in relation to the allegations levelled against them. Nor would it assist them in the exercise or protection of their rights.[34] According to the court, the applicants effectively were seeking to embark on a 'full-scale forensic audit'[35] of the Company — an ordering of the production of the documents was likely to escalate the matter into a 'full-blown, costly, elaborate and lengthy exercise'[36] which, the court asserted, is not what was envisaged by s 71(4)*(a)* of the Companies Act.[37]

Consequently, the court ruled that the Company had met the 'sufficient specificity' requirement in s 71(4)*(a)* of the Companies Act — the applicants had been given sufficiently detailed reasons to mount a response to the allegations levelled against them. The court thus dismissed the applicants' application for the additional documents, with costs.[38] In the final event, the court pointed out that if the applicants were dissatisfied with the board's determination to remove them as directors, they could avail themselves of s 71(5) of the Companies Act, in terms of which they could apply for the board's decision to be reviewed by a court of law.[39]

V CONTESTING THE REMOVAL OF DIRECTORS BY THE BOARD OF DIRECTORS

There are three main avenues which a director may pursue in order to contest his removal from the board of directors by the board of directors. The first avenue is to make a presentation to the board of directors in order to convince the board not to vote in favour of his removal. The second avenue is to apply to a court of law to review the board of directors' decision to remove him from the board. The final avenue is to sue the company for damages or other compensation for loss of office as a director. These avenues, as well as their level of effectiveness, are discussed below.

(a) Presentation

As discussed earlier, before the board of directors may consider a resolution to remove a director, the director concerned must be given a copy of the proposed resolution and a statement setting out the reasons for the resolution with sufficient specificity to permit the director reasonably to prepare and present a response to the board of directors.[40] The director concerned must be given a reasonable opportunity to make a presentation to the board, either in person himself or through a representative, before votes are cast on the resolution to remove him as a director.[41] The purpose of this presentation is

[34] Ibid.
[35] Ibid para 45.
[36] Ibid.
[37] Ibid.
[38] Ibid para 49.
[39] Ibid para 48.
[40] Section 71(4)*(a)* of the Companies Act.
[41] Section 71(4)*(b)* of the Companies Act.

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to give the director concerned an opportunity to state his case, to prevent him from being removed from office on an impulsive vote.

As stated previously, the phrase in s 71(3) 'must determine the matter by resolution' indicates that if any director or shareholder alleges that a particular director is ineligible, disqualified, incapacitated, negligent or derelict in his functions, the board of directors is obliged to determine the matter by resolution. Thus, even if a single shareholder or director makes vexatious and/or groundless allegations against a director, the issue of removal of the director has to be determined by the board of directors.[42] Furthermore, as indicated by the phrase 'may remove a director' in s 71(3), the board of directors has a discretion whether or not to remove the director in question. Thus, if a director wishes to contest his proposed removal from office, the opportunity to make a presentation to the board is critically important, particularly where he is of the view that the allegations made are vexatious.

(i) *The 'sufficient specificity' standard*

In order to prepare for his presentation to the board of directors, a director would have to respond to the statement of reasons for his removal, and these reasons are required by s 71(4)*(a)* of the Companies Act to be described with 'sufficient specificity'. It is not clear from s 71(4)*(a)* what exactly would constitute 'sufficient specificity', and how much detail would have to be provided in order to meet the 'sufficient specificity' standard. The interpretation of the words 'sufficient specificity' was considered by the Western Cape High Court in *Pretorius*.

As discussed above, in finding that the documents sought by the applicants would not assist them in exercising or protecting their rights, the court in *Pretorius* was influenced by the fact that the allegations made in the statement of reasons for the applicants' removal as directors were simple, uncomplicated, comprised largely of eyewitness testimony and did not allege that the applicants had been guilty of 'complex commercial fraud'.[43] The principles which emerge from *Pretorius* are that the question whether the statement setting out the reasons for the proposed removal of a director would meet the 'sufficient specificity' standard depends on the facts of the particular case, and more specifically, on the complexity of the reasons provided for the director's proposed removal from the board of directors. Accordingly in a complicated case, detailed reasons, information and documentation must be produced by a company in order to meet the standard of 'sufficient specificity', while in a simpler case, fewer reasons, information and documentation would be required. The court in *Pretorius* also stated that s 71(4)*(a)* of the Companies Act does not envisage a full-scale forensic audit of the company or that the parties in question would engage in a 'full-blown, costly, elaborate and

[42] It is not required by s 71(3) of the Companies Act that the allegation be made in writing. Presumably, the allegation could be made verbally, for instance, at a shareholders' meeting or a board meeting (see Cassim et al op cit note 9 at 444).

[43] Supra note 1 para 44.

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lengthy exercise'.[44] However, if a company were to allege that a director is guilty of complex commercial fraud, then, according to *Pretorius*, such a company may nonetheless have to engage in a more elaborate and costly exercise in order to meet the 'sufficient specificity' requirement of s 71(4)*(a)* of the Companies Act.

The question arises whether the Western Cape High Court in *Pretorius* correctly interpreted the phrase 'sufficient specificity' in s 71(4)*(a)* of the Companies Act. As I pointed out in part IV, the court relied on the judgment in *Avril* to interpret the phrase 'sufficient specificity' in s 71(4)*(a)* of the Companies Act. However, *Avril* was a decision of the Labour Court regarding the dismissal of an employee by her employer. In dealing with the concept of procedural fairness in the LRA, the Labour Court found that the Explanatory Memorandum that accompanied the Draft Labour Relations Bill presaged an informal approach to procedural fairness.[45] The Explanatory Memorandum to the Draft Labour Relations Bill provides as follows:

> 'The draft Bill requires a fair, but brief, pre-dismissal procedure. . . . [It] opts for this more flexible, less onerous, approach to procedural fairness for various reasons — small employers, of whom there are a very large number, are often not able to follow elaborate pre-dismissal procedures; and not all procedural defects result in substantial prejudice to the employee.'[46]

In *Avril*, the Labour Court interpreted the approach outlined in the Explanatory Memorandum to the Draft Labour Relations Bill as meaning, in the context of dismissals of employees, that there is no place for formal disciplinary procedures that incorporate all the accoutrements of a criminal trial, such as the leading of witnesses, technical and complex charge sheets, requests for particulars, the application of the rules of evidence, legal arguments and so forth.[47] The court in *Pretorius* relied on this pronouncement in *Avril* to interpret the phrase 'sufficient specificity' in s 71(4)*(a)* of the Companies Act.[48] The Labour Court in *Avril* further emphasised that the informal rules relating to procedural fairness in the LRA recognise that for employees, 'true justice lies in a right to an expeditious and independent review of the employer's decision to dismiss, with reinstatement as the primary remedy when the substance of employer decisions are found wanting'.[49] This rationale has little relevance to s 71 of the Companies Act.

Notably, in interpreting the phrase 'sufficient specificity' in s 71(4)*(a)*, the court in *Pretorius* failed to consider the provisions of s 5(1) of the Companies Act. In terms of s 5(1), the Companies Act must be interpreted and applied in a manner that gives effect to the purposes set out in s 7 of the Companies Act.

[44] Ibid para 45.
[45] Supra note 25 at 839.
[46] 'Explanatory memorandum to the draft Labour Relations Bill' published in (1995) 16 *ILJ* 278 at 317.
[47] Supra note 25 at 839.
[48] Supra note 1 para 10.
[49] Supra note 25 at 839.

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Thus, in interpreting the phrase 'sufficient specificity' in s 71(4)*(a)*, the court was statutorily required to consider and give effect to the purposes of the Companies Act. Whilst s 7 sets out several purposes, two purposes in particular stand out in this context which, perhaps, ought to have been considered by the court in *Pretorius*. The first would be the purpose of promoting the development of the South African economy by encouraging transparency and high standards of corporate governance.[50] The second would be the purpose of encouraging the efficient and responsible management of companies.[51] It is thus arguable that these purposes require more detailed reasons and information be given to a director who is about to be removed by the board of directors than that envisaged by the court in *Pretorius*. Providing directors with detailed reasons and information, even when the allegations against them are basic and simple, would encourage transparency and the efficient and responsible management of companies. Perhaps, if the court had taken account of these purposes in interpreting the phrase 'sufficient specificity', as opposed to the purposes and background of the LRA only, it may have found that there is place for more procedural formalities under s 71(4)*(a)* of the Companies Act as compared to that envisaged under the LRA.

In addition, it is questionable whether the court in *Pretorius* ought to have adopted the philosophy of procedural fairness in regard to dismissals under the LRA in the first place. The respective backgrounds, developments and purposes under the LRA and the Companies Act are diverse. The LRA is concerned mainly with the interests of employees, the promotion of job security and the continuity of employment. Moreover, the LRA is designed primarily to regulate employment relations between blue collar workers and their employers. This can be gleaned from the many sections and schedules of the Act pertaining to collective bargaining, collective agreements, the status of unions, retrenchments and so forth.[52] By contrast, company law serves quite a different purpose. Traditionally, it is concerned with the interests of the shareholders of the company, and with the balancing of the rights and obligations of shareholders and directors within companies.[53]

While the respective procedures to dismiss an employee under the LRA and to remove a director under the Companies Act contain some similarities, there are important differences between the two procedures, particularly in regard to the consequences of a finding of unfair dismissal of an employee and the unfair removal of a director. The similarities are that in both instances, the individual in question must be given an opportunity to present his case in response to the allegations, and must have access to the assistance of a

[50] Section 7*(b)*(iii) of the Companies Act.

[51] Section 7*(j)* of the Companies Act.

[52] See *PG Group (Pty) Ltd v Mbambo* [2005] 1 BLLR 71 (LC) para 22.

[53] See s 7*(i)* of the Companies Act and BPS van Eck & S Lombard 'Dismissal of executive directors: Comparing principles of company law and labour law' 2004 *TSAR* 20 at 23.

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representative.[54] After the dismissal, an employee would have a right to refer the matter to a bargaining council with jurisdiction, the Commission for Conciliation, Mediation and Arbitration, or any dispute resolution procedure established in terms of a collective agreement.[55] In a similar vein, after the removal of a director from the board of directors of a company, a director would have a right to apply to a court of law, within twenty business days of his removal, to review the determination of the board of directors.[56]

At the same time, however, there are important differences between the two procedures. In the case of a finding of an unfair dismissal of an employee, a court or arbitrator must order the employer to reinstate or re-employ the employee,[57] unless the employee does not wish to be reinstated or re-employed, the circumstances surrounding the dismissal are such that a continued employment relationship would be intolerable, it is not reasonably practicable for the employer to reinstate the employee, or the dismissal is unfair only because the employer did not follow a fair procedure.[58] In the latter instances, the court or the arbitrator may instead order the employer to pay compensation to the employee,[59] which compensation must be just and equitable in the circumstances and may not be more than the equivalent of twelve months' remuneration, calculated at the employee's rate of remuneration on the date of dismissal.[60]

By contrast, s 71(5) of the Companies Act does not specify the order(s) which a court may make if, on review of a board's decision to remove a director, it finds that the removal was unfair. Unlike the case of an employee, it is not clear whether a court could or would in fact order the reinstatement of a director. Furthermore, while an employee who has been unfairly dismissed would be entitled to compensation, s 71(5) of the Companies Act makes no express provision for the compensation of an unfairly removed director. The Companies Act has also not provided any guidance as to how such compensation would be calculated.

If, on the interpretation of the phrase 'sufficient specificity' in *Pretorius*, a director is entitled only to limited information, it would be challenging for him to prepare and present a presentation to the board of directors before the resolution to remove him is put to the vote. In light of this, would he have any right to inspect the books and records of the company in order to assist him to prepare his presentation to the board of directors to contest his proposed removal? As the Singapore Court of Appeal in *Wuu Khek Chiang George v ECRC Land Pte Ltd*[61] stated, the right to inspect the books and records of the company is an important right because 'the books and records

[54] See s 71(4)*(b)* of the Companies Act and item 4(1) of the Code of Good Practice.
[55] See item 4(3) of the Code of Good Practice.
[56] Section 71(5) of the Companies Act.
[57] Section 193(1)*(a)* and *(b)* of the LRA.
[58] Section 193(2) of the LRA.
[59] Section 193(1)*(c)* of the LRA.
[60] Section 194(1) of the LRA.
[61] [1999] 3 SLR 65.

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of a company are a primary, and sometimes the only, source of information as to the state of affairs of a company'.[62] The right of a director to inspect the books and records of a company will be examined below.

(ii) *The right of directors to inspect the books and records of a company*

(aa) The statutory right to inspect the books and records of a company

As discussed above, the applicants in *Pretorius* sought access to various records of the company, including certain financial statements, stock sheets, purchase invoices, value-added tax invoices and monthly management accounts of the company. The court found that the applicants were not entitled as of right, in their capacities as directors, to the requested documents.[63] Notably, the Companies Act does not give directors a statutory right to inspect the records of a company. Section 26 gives shareholders of a company (and members of a non-profit company) a right to inspect and copy certain records of a company. Yet, this provision does not extend to the directors of a company.

In sharp contrast, s 284(3) of the Companies Act of 1973 provided that the accounting records of a company were open to inspection by the directors at all times. However, the right of inspection conferred by s 284(3) of the Companies Act of 1973 was not absolute. In *Wes-Transvaalse Boeresake (Edms) Bpk v Pieterse*,[64] the court accepted that such a statutory provision conferred a statutory right of inspection of the books and accounts of a company upon a director, but that this was not an unqualified right or a right that was absolutely exercisable in all circumstances.[65] Nevertheless, in *Conway v Petronius Clothing Co Ltd*[66] ('*Conway*') the court held that the equivalent section in the English Companies Act of 1948 did not in fact confer a statutory right of inspection. Rather, the right was conferred in terms of the common law.[67] Be that as it may, the question whether the right is a statutory one or one that is conferred only at common law is no longer of relevance because an equivalent provision to that of s 284(3) of the Companies Act of 1973 has not been included in the new Companies Act.

(bb) The common-law right to inspect the books and records of a company

While directors may no longer have a statutory right to inspect the books and records of a company, they do have a common-law right to do so.[68] The common-law right enables a director to perform his duties as a director and

[62] Ibid para 33.

[63] Supra note 1 para 28.

[64] 1955 (2) SA 464 (T). In this case, the court was commenting on the equivalent section in the Companies Act 46 of 1926.

[65] Ibid at 467–8.

[66] [1978] 1 All ER 185.

[67] Ibid at 202.

[68] *Conway* supra note 66 at 201; M S Blackman, R D Jooste, G K Everingham et al *Commentary on the Companies Act* vol 2 (2011) (Revision Service 8) at 8-26 ('Blackman et al').

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to fulfil his duties for the benefit of the company.[69] Since the books and records of a company are a primary source of information as to the state of affairs of a company, it follows that unless a director has access to these sources of information, he would be severely inhibited in the proper performance of his duties.[70] These duties include the protection of the interests of the company and its shareholders.[71] Importantly, if a director were to invoke the right to inspect the books and records of a company for a purpose other than that of carrying out his duties as a director, this would constitute an improper purpose.[72]

Since the right to inspect the books and records of a company is not a statutory right, a court has a discretion whether or not to order such inspection.[73] Although a director generally will not be called on to furnish reasons before being allowed to exercise his right of inspection, as the court in *Conway* stated, a court would 'restrain him in the exercise of the right, if satisfied affirmatively that his intention was to abuse the confidence reposed in him as director and materially to injure the company'.[74] Likewise, in *Oxford Legal Group Ltd v Sibbasbridge Services Ltd*,[75] the Court of Appeal maintained that if a director were to invoke the right to inspect for a purpose other than that of carrying out his duties as a director, this would constitute an improper purpose and a court would not intervene to assist him.[76] An example of an improper purpose would be where a director seeks to inspect the books and records of a company for the benefit of a competitor.[77] The onus of proving that the inspection was sought for an improper purpose rests with those who oppose the inspection by the director,[78] and in the absence of clear proof to the contrary, a court would assume that the director was seeking to exercise the right of inspection for the benefit of the company.[79]

In *Pretorius*,[80] the applicants had argued that they were entitled to inspect the documents requested by them in their capacities as directors in order to manage the business and affairs of the company. However, the court found that the applicants had required the documents not to protect the Company but rather to protect themselves as directors and to safeguard themselves from possible removal from the board of directors.[81] While the court in *Pretorius*

[69] *Conway* supra note 66 at 201–2; *Wuu Khek Chiang George v ECRC Land Pte Ltd* supra note 61 para 33; *Oxford Legal Group Ltd v Sibbasbridge Services Ltd* [2008] EWCA Civ 387 para 23.

[70] *Wuu Khek Chiang George v ECRC Land Pte Ltd* supra note 61 para 33.

[71] *Oxford Legal Group Ltd v Sibbasbridge Services Ltd* supra note 69 para 33.

[72] Ibid para 23.

[73] Blackman et al op cit note 68 at 8-26.

[74] *Conway* supra note 66 at 201.

[75] Supra note 69.

[76] Ibid para 24.

[77] Ibid para 49.

[78] Ibid para 43; *Conway* supra note 66 at 201.

[79] *Conway* supra note 66 at 201.

[80] Supra note 1 para 22.

[81] Ibid paras 23 and 27.

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did not discuss the common-law right of inspection given to directors in any detail, the court appeared to exercise its discretion against the applicants' request for inspection because their request had been made for an improper purpose.[82]

In regard to whether a court would exercise its discretion to allow a director, who is about to be removed from the board of directors, to inspect the books of a company, Slade J in *Conway* asserted that where there is no reason to suppose that a director is about to be removed from office, the discretion to withhold an order for inspection will be exercised very sparingly.[83] In other words, where a director is about to be removed from office, a court may well exercise its discretion to withhold an order of inspection. However, the court did not make a prospective vote of removal an absolute bar to an inspection order — each case must depend on its own special facts. The court commented further that it is conceivable that in particular circumstances, a court may consider it essential for the protection of the company or the personal protection of the director that he be allowed to inspect the company's books notwithstanding his impending removal from office.[84]

Prentice has criticised this position. He has questioned whether a prospective removal of a director should indeed be allowed to curtail his right of inspection.[85] Prentice contends that a prospective vote to remove a director from office should be ignored when a court exercises its discretion whether to grant an order for inspection of the company's books because 'often[,] it may be nothing more than a tactical move by wrongdoers to stifle a conscientious director'.[86] Even though Slade J did not make a prospective removal vote an absolute bar to an inspection order, Slade J did appear to put the onus on the director concerned to show that his right of inspection is necessary in order to protect the company, as Prentice argues.[87] This is in contrast to the general position, as discussed above, that a director will not be called on to furnish reasons before being allowed to exercise his right of inspection. It is also inconsistent with the onus being on the person who asserts that the right is being exercised for an improper purpose to establish this. Moreover, as Prentice points out, it may well be the case that a director would only be able to show that the order of inspection is necessary for the protection of the company after he has perused its books.[88]

It is submitted that in exercising its discretion to grant an order of inspection under the common law, a court should consider carefully whether a prospective vote of removal of a director is indeed a tactical manoeuvre to

[82] See *Pretorius* supra note 1 para 27.
[83] Supra note 66 at 201.
[84] Ibid at 202.
[85] See D D Prentice 'A director's right of access to corporate books of account' (1978) 94 *LQR* 184 at 186.
[86] Ibid.
[87] Ibid.
[88] Ibid.

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stifle a conscientious director. A court should not be too hasty in refusing access to the company's records to a director whose removal may be proposed by the board of directors.

(cc) The right to inspect the books and records of a company in terms of PAIA

Regulation 24 of the Companies Regulations, 2011 provides that any right of access of any person to any information contemplated in s 26 of the Companies Act or in Regulation 24, may be exercised only in accordance with PAIA or the provisions of s 26 of the Companies Act. In addition, a completed Request for Access to Information in Form CoR24 (Request for Access to Company Information) must be delivered to the company, together with any further documents or material required in terms of PAIA.

In *Pretorius*, the applicants had relied on s 50 of PAIA in order to inspect certain documents and records of the Company. In terms of s 50(1) of PAIA, a requester must be given access to any record of a private body if (a) that record is required for the exercise or protection of any rights; (b) that person complies with the procedural requirements of PAIA relating to a request for access to that record; and (c) access to that record is not refused in terms of any ground for refusal contemplated in Chapter 4 of Part 3 of PAIA.

In regard to the first requirement, the Supreme Court of Appeal ('SCA') stated in *Claase v Information Officer, South African Airways (Pty) Ltd*[89] that an applicant is not required to establish a clear right worthy of protection. He is required merely to 'put up facts which *prima facie*, though open to some doubt, establish that he has a right which access to the record is required to exercise or protect'.[90] In *Cape Metropolitan Council v Metro Inspection Services (Western Cape) CC*,[91] the SCA formulated a test to determine whether information would be required for the exercise or protection of any rights, as follows:

> 'Information can only be required for the exercise or protection of a right if it will be of assistance in the exercise or protection of the right. It follows that, in order to make out a case for access to information . . . an applicant has to state what the right is that he wishes to exercise or protect, what the information is which is required and how that information would assist him in exercising or protecting that right.'[92]

The meaning of the term 'required' in s 50(1)*(a)* of PAIA is neither clear nor precise, and courts have struggled to give the term practical content.[93] In *Unitas Hospital v Van Wyk*,[94] the SCA stated that, generally speaking, the question whether a particular record is 'required' for the exercise or protection of a particular right is inextricably bound up with the facts of the

[89] 2007 (5) SA 469 (SCA).
[90] Ibid para 8.
[91] 2001 (3) SA 1013 (SCA).
[92] Ibid para 28.
[93] *Unitas Hospital v Van Wyk* 2006 (4) SA 436 (SCA) paras 16 and 30.
[94] Ibid.

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matter.[95] In this case,[96] the SCA adopted the formulation of the term 'required' in s 50(1)*(a)* of PAIA as advocated for in the earlier case of *Clutchco (Pty) Ltd v Davis*,[97] where it stated:

> 'I think that "reasonably required" in the circumstances is about as precise a formulation as can be achieved, provided that it is understood to connote a substantial advantage or an element of need. It appears to me, with respect, that this interpretation correctly reflects the intention of the Legislature in s 50(1)*(a)*.'[98]

In applying this formulation in *Claase*, the SCA found that the substantial advantage in that case was that the information requested would be decisive and would bring a 'short sharp end to the dispute'.[99]

In applying the test set out in *Cape Metropolitan Council v Metro Inspection Services (Western Cape) CC*[100] in *Pretorius*, it was found that the first two legs of the test had been satisfied because the applicants had stated the right which they wished to exercise or protect (i e the right to safeguard their removal as directors of the Company) and that they had also set out the information that was required.[101] However, the court found that the applicants had failed to satisfy the third leg of the test — the applicants had failed to show the manner in which the information would assist them in exercising or protecting that right. In other words, they had failed to satisfy the element of need.[102] It was not sufficient for the applicants to show that they had a prima facie right of protection — they also had to explain the relevance of each document upon which they intended to rely.[103]

In light of the fact that the allegations made against the applicants in *Pretorius* had been simple and uncomplicated, the court found that the production of the financial and commercial records of the Company, as sought by the applicants, would not assist them in a meaningful way in relation to the allegations levelled against them. Nor would it assist them in exercising or protecting their rights.[104] The court held that the production of the documents sought by the applicants would not bring the dispute to a 'short, sharp end'[105] and so provide the applicants with a substantial advantage in the sense that it would be decisive of the matter.[106] Accordingly, the court ruled that the applicants had been provided with sufficiently detailed reasons to mount a response to the allegations levelled against them

[95] Ibid para 6.
[96] Ibid paras 17–18.
[97] 2005 (3) SA 486 (SCA).
[98] Ibid para 13.
[99] Supra note 89 para 9.
[100] Supra note 91.
[101] Supra note 1 para 33.
[102] Ibid.
[103] Ibid para 31.
[104] Ibid para 44.
[105] Ibid para 45.
[106] Ibid.

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and thus dismissed their application for access to the additional documents.[107] It was not necessary for the court to consider the Company's defence of sensitive commercial information in accordance with s 68 of PAIA.

As may be seen from the application of the requirements of s 50 of PAIA in *Pretorius*, the requirements are specific. So, unless a director who is about to be removed from the board of directors is successful in relying on the common-law right to inspect the books and records of a company, he would have to satisfy these stringent requirements under s 50(1) of PAIA if he wishes to access the books and records of the company in order to prepare his presentation to the board of directors.

(iii) *Verbal presentation*

In terms of s 220(3) of the Companies Act of 1973, a director could have been removed by the shareholders. Notably, the director concerned could make written representations to the shareholders and request that the shareholders be notified of his written representations prior to the date of the meeting. In order for this request to be complied with, the written representations had to have been received by the company timeously, had to have been of a reasonable length and not defamatory.[108] In contrast, s 71 of the Companies Act does not make any provision for a director to make written representations to the board of directors (or to the shareholders). The director (or his representative) may only make verbal representations at the board meeting.

This has the implication that the board of directors (and the shareholders) would not have an opportunity to consider the director's defence prior to the meeting to vote on his removal. Accordingly, the board of directors (and the shareholders) would have to decide at the meeting whether to accept the defence advocated by the director (or his representative) in his verbal presentation. While the right of a director under s 71(4)*(b)* to make a verbal presentation to the board of directors (and the shareholders) before the resolution is put to a vote allows him to state his case and to contest his impending removal, the fact that the board of directors (and the shareholders) is not given an opportunity carefully to consider his defence prior to the meeting, or to verify his defence to their satisfaction, would put the director concerned at a distinct disadvantage. This disadvantage is more acute when a director is to be removed by the shareholders of a company as opposed to the board of directors, because the board of directors is generally a more coherent group than the shareholders and would be more closely involved in the removal of a director.

(b) An application to court to review the decision of the board of directors

As the court pointed out in *Pretorius*,[109] s 71(5) of the Companies Act enables a director who is dissatisfied with the determination of the board of directors

[107] Ibid para 46.
[108] Section 220(3) and (5) of the Companies Act of 1973.
[109] Supra note 1 para 48.

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to remove him, to apply to a court of law within twenty business days to review the determination. Section 71(5) uses the term 'review' and not the term 'appeal'. Even so, it is not clear whether a court would be empowered to review the substance and merits of the board's decision or whether it would be empowered to review only the procedural aspects of the decision.

In the strict traditional sense, the substance of a decision is examined on an appeal — an appeal is a reconsideration of, and a fresh determination on the merits of the matter, but it is limited to the evidence or information on which the original decision was given.[110] By contrast, a review involves an enquiry into the procedural aspects of the decision.[111] The question in an appeal is whether the decision was right or wrong,[112] while the question in a review is whether the procedure adopted was formally correct or whether there were irregularities in the proceedings which may show that there has been 'a failure of justice'.[113] Accordingly, on a strict traditional reading of s 71(5) of the Companies Act, a court reviewing the decision of the board of directors to remove a director would be empowered only to enquire into the procedural correctness of the decision and not the substance of the decision.

By contrast, s 71(6) of the Companies Act provides that when a court 'reviews' a decision of the board of directors *not* to remove a director, it would be empowered to examine the substance of the decision and not just the procedural aspects of the decision. In terms of s 71(6), a court reviewing a decision where the board has decided *not* to remove a director can either confirm the decision of the board, or remove the director from office if the court is 'satisfied' that the director is ineligible, disqualified, incapacitated or has been negligent or derelict. The word 'satisfied' indicates that, in reviewing the board's decision not to remove a director, a court would be empowered to consider the merits of the matter, and not just the procedural aspects of the decision.[114] While this is not conclusive, an argument may be made that a court reviewing the decision of the board of directors under s 71(5) of the Companies Act would likewise be empowered to consider both the merits and the procedural aspects of the decision.

It is also notable that in terms of s 70(2) of the Companies Act, if the board of directors has removed a director, a vacancy on the board does not arise until the later of the expiry of the time for filing an application for review in terms of s 71(5) or the granting of an order by the court on such an application. However, the director in question would be suspended from his

[110] *Tikly v Johannes NO* 1963 (2) SA 588 (T) at 590–1; *Health Professions Council of SA v De Bruin* [2004] 4 All SA 392 (SCA) para 23; *Samancor Group Pension Fund v Samancor Chrome* 2010 (4) SA 540 (SCA) para 15.

[111] *Tikly v Johannes NO* supra note 110 at 590–1.

[112] Ibid; *Thuketana v Health Professions Council of South Africa* 2003 (2) SA 628 (T) at 634–5.

[113] *Tikly v Johannes NO* supra note 110 at 591; *Davies v Chairman, Committee of the Johannesburg Stock Exchange* 1991 (4) SA 43 (W) at 48.

[114] See Ncube op cit note 11 at 47.

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office during that time.[115] Section 70(2) applies only to the removal of a director by the board of directors under s 71(3) and does not pertain to the removal of a director by the Companies Tribunal.[116] This may be an oversight or unintended consequence on the part of the legislature.

Where a director is removed from the board of directors due to ulterior motives, and thus in breach of the individual directors' fiduciary duties, this would likely be taken into account by a court in the course of a review under s 71(5) of the Companies Act.[117] However, the difficulty faced by the director being removed is that he would bear the onus of proving, on a balance of probabilities, that the board of directors made its decision with ulterior motives. A mere suspicion in this regard would not be sufficient. This may be challenging for the affected director, particularly considering that the board may frame the grounds for his removal as him having neglected his functions or been derelict in the performance of his functions, or that he failed to meet a broadly expressed or subjective standard.[118]

As pointed out above, s 71(5) of the Companies Act does not indicate the order that a court may make if, on review, it sets aside the board of directors' decision to remove the director. The court in *PG Group (Pty) Ltd v Mbambo*[119] stated that in light of the dual capacities in which an executive director holds office, it is questionable whether a court could or would order the reinstatement of a director who had been unfairly removed,[120] or whether this would even be practical. It is also not clear whether a court would be empowered under s 71(5) of the Companies Act to order compensation to such a director, and if so, the basis upon which the compensation would be calculated. The Explanatory Memorandum to the Draft Labour Relations Bill states that, in the absence of statutory guidelines or caps on compensation, the courts have used tests applied in personal injury claims to assess the losses of employees.[121] However, such tests are not appropriate in calculating the amount of compensation to be awarded to directors who have been unfairly removed from office by the board of directors. Even if, on review, a court were to find that a director's removal from the board of directors was invalid, this may not entirely alleviate the embarrassment or humiliation a director may have suffered on his removal from office by his fellow board members.

(c) An application for damages or other compensation

Section 71(9) of the Companies Act provides that nothing in s 71 would deprive a person removed from office as a director in terms of s 71 of any

[115] Section 70(2) of the Companies Act.
[116] See Ncube op cit note 11 at 46.
[117] Cassim et al op cit note 9 at 447; Cassim op cit note 11 at 164.
[118] See Austin & Ramsay op cit note 13 at 263 para 7.240.
[119] Supra note 52.
[120] Ibid para 29.
[121] See the 'Explanatory memorandum to the draft Labour Relations Bill' op cit note 46 at 316 and 320.

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right that he may have at common law or otherwise, to apply to a court of law for damages (or other compensation) for the loss of office as a director. Thus, where a company has appointed a director for a fixed period and that period has not expired at the time the director is removed from office, or the company has agreed to compensate a director in the event of his removal from office, the affected director may claim damages (or other compensation) from the company.[122]

Notably, in terms of s 15(6)*(c)*(i) of the Companies Act, the Memorandum of Incorporation of a company is now binding between the company and each director of the company. Consequently, it is no longer necessary for a director to have a separate contract of service in order to apply to a court of law under s 71(9). The director would be able to rely on a breach of the Memorandum of Incorporation if his removal from office were to result in a breach of one or more of its provisions.[123] Where, however, the affected director has breached the Memorandum of Incorporation or his contract of service in a manner which entitles the company to cancel its contract with him, he would have no action for damages against the company for his loss of office as a director.[124]

A claim for damages (or other compensation) may also be brought for the loss of any other office as a consequence of being removed as a director. For instance, if the removal of the person breaches a second contract, which the person could perform only by being a director, such as that of a managing director, a claim for the loss of the office of managing director may also be brought under s 71(9) of the Companies Act.[125]

The director concerned would have the onus of proving his damages (or other compensation) for his loss of office as a director and for his loss of any other office as a consequence of being removed as a director. These damages are potentially quite high. For instance, in *Bold v Brough, Nicholson & Hall Ltd*,[126] a director who had served the company for forty years had been wrongfully dismissed both as a director and as the managing director of the company. The company had agreed to appoint the director in question as managing director for ten years, but after approximately three years, the company had summarily and wrongfully removed the director from this position. The damages awarded by the court included loss of salary, loss of commission on the profits of the company, diminution in the pension he would have received under the staff pension and assurance scheme, loss of life insurance cover under the scheme, the amount of premiums payable under the company's discretionary pension and life assurance scheme which the

[122] See Blackman et al op cit note 68 at 8-285.

[123] See further Cassim et al op cit note 9 at 452.

[124] Blackman et al op cit note 68 at 8-286; Cassim op cit note 11 at 167.

[125] See *Southern Foundries (1926) Ltd v Shirlaw* [1940] AC 701 and *Schindler v Northern Raincoat Co Ltd* [1960] 2 All ER 239.

[126] [1953] 3 All ER 849. For a further discussion of this case, see Cassim op cit note 11 at 166–7.

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company had undertaken to pay on behalf of the director in question, as well as interest on the total amount of damages awarded.

While the right to institute an action for damages (or compensation) for the loss of office would not result in a director being reinstated to the board of directors, the fact that he has such a right would serve to focus the mind of the board of directors when considering whether to vote in favour of or against removing him from the board, particularly where the damages he would be able to claim for the loss of his office would be quite high.

VI AUTOMATIC TERMINATION PROVISIONS

A further point of interest that arises from *Pretorius* relates to automatic termination provisions. It is well established that relying on an automatic termination provision to bring an end to an employment relationship automatically once an individual has been removed as a director of a company, is not legally permissible.[127] An executive director holds a position both as a director and as an employee. Thus, if he ceases to be a director, a clause in his employment contract stating that his employment would terminate automatically, may not be relied upon because that individual may not be deprived of his employment law rights under the LRA.

In *Pretorius*, the court was faced with the opposite scenario — that is, a situation where the directors had resigned as employees and a clause in their service contracts had provided that in the event of termination of their employment, they would be required also to resign as directors on request by the Company. The applicants alleged that this clause had been included in their service agreements as a result of a common mistake, which the Company denied.[128] From the facts of the judgment, it is not clear why the respondents had not taken steps to enforce this particular clause in the applicants' service agreements instead of initiating proceedings under s 71 of the Companies Act. Further, the court did not deal with the validity of such a clause. It did not even allude to the issue.

Section 71(3) of the Companies Act does not expressly or impliedly state whether additional grounds for the removal of a director may be included in the company's Memorandum of Incorporation or in a director's service contract. By contrast, s 220(7) of the Companies Act of 1973 provided that, '[n]othing in this section shall be construed as . . . derogating from any power to remove a director which may exist apart from this section'. An equivalent provision to s 220(7) of the Companies Act of 1973 has not been included in the Companies Act.

However, it is arguable that additional grounds for the removal of a director may be included in the Memorandum of Incorporation in terms of s 15(2)*(a)*(ii) of the Companies Act. Section 15(2)*(a)*(ii) provides that the Memorandum of Incorporation of a company may impose on the company a

[127] *Chillibush v Johnston* [2010] 6 BLLR 607 (LC); *SA Post Office Ltd v Mampeule* [2010] 10 BLLR 1052 (LAC).

[128] See *Pretorius* supra note 1 para 3.

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higher standard, greater restriction, longer period of time or any similarly more onerous requirement than would otherwise apply to the company in terms of an unalterable provision of the Companies Act. It is submitted that the additional grounds contemplated here could well qualify under this provision.[129]

Furthermore, s 69(6) of the Companies Act provides that the Memorandum of Incorporation of a company may impose additional grounds of ineligibility or disqualification of directors. In addition, s 71(3) states that if a shareholder or director alleges that a director 'has become ineligible or disqualified in terms of section 69', the board must determine the matter by resolution. Accordingly, it would seem that additional grounds for removal of a director may be included in a company's Memorandum of Incorporation if these grounds constitute additional grounds of ineligibility or disqualification, and that the procedures under s 71(3) and (4) must be used to remove such a director from office. To use the facts of *Pretorius* as an example, the Memorandum of Incorporation may provide that a director would be disqualified from being a director of the company if he ceases to be an employee. Consequently, if a director of this company is dismissed lawfully as an employee, or resigns as an employee, he would be disqualified from being a director, and could then be removed by the board of directors in accordance with the procedures set out in s 71(3) and (4).

VII AN APPLICATION TO DECLARE A DIRECTOR DELINQUENT

Under s 162(2) of the Companies Act, various persons have locus standi to apply to court for an order declaring a person delinquent, including the company, a shareholder and a director. In terms of s 162(5) of the Companies Act, a court must make an order declaring a person a delinquent director if, inter alia, the person acted in the capacity of a director while ineligible or disqualified in terms of s 69 of the Companies Act; grossly abused his position as a director; took personal advantage of information or an opportunity or intentionally or by gross negligence inflicted harm on the company or its subsidiary while a director (contrary to s 76(2)*(a)*), or while a director acted in a manner that amounted to gross negligence, wilful misconduct or breach of trust or in a manner contemplated in s 77(3) *(a)*, *(b)* or *(c)* (unauthorised acts, reckless trading or fraud). Section 162 of the Companies Act is directed at protecting companies and corporate stakeholders against company directors who proved themselves unable to manage the business of the company or have failed in, or are in neglect of their duties and obligations as directors of a company.[130] The effect of an order of delinquency is that the person is disqualified from being a director of the company, with the automatic result

[129] Despite the provisions of s 15(2)*(a)*(ii) of the Companies Act, in terms of s 65(8) of the Companies Act the threshold for passing an ordinary resolution may not be increased in the case of the removal of a director under s 71 of the Companies Act.

[130] *Msimang NO v Katuliiba* [2013] 1 All SA 580 (GSJ) para 29.

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that a director who has been declared delinquent would be removed from office.[131] Depending on the grounds of disqualification, the order may be conditional or unconditional and may subsist for seven years or longer, as determined by the court.[132]

One of the reasons provided in the statement of reasons for the proposed removal of the applicants as directors in *Pretorius* was that they had made a secret profit unlawfully from a sale of certain products which ought to have accrued to the Company. It is noteworthy that, based on this ground and the evidence available to prove this allegation, the board of directors could have applied for an order declaring the applicants delinquent directors. This was so on the ground that they had grossly abused their positions, or had taken personal advantage of information or an opportunity, or, possibly, that they had intentionally inflicted harm upon the Company. This would have had the automatic effect of the applicants being removed as directors of the Company, and more significantly, would have avoided the potential complexity of removal of a director in terms of s 71 of the Companies Act. It is not clear why the Company did not adopt this course of action.

VIII CONCLUSION

In *Pretorius*, the court made it clear that s 71(4)*(a)* of the Companies Act does not envisage a full-scale forensic audit of the affairs of the company when a director requests further reasons for his proposed removal from the board of directors. The principle which emerges from *Pretorius* is that the 'sufficient specificity' standard in s 71(4)*(a)* entails that each case must be decided on its own facts, but that the more complex the reasons for the removal of a director from office, the more detailed the information to which the director is entitled. It is submitted that the court may have come to a different conclusion on the interpretation of the phrase 'sufficient specificity' had it considered the purposes of the Companies Act set out in s 7, as it is required to do in terms of s 5(1) of the Companies Act. It is submitted further, that in light of the differences in the philosophies underlying the LRA and the Companies Act, as well as the differences in their respective dismissal and removal procedures, it is questionable whether the court in *Pretorius* adopted the correct approach when it relied on the LRA jurisprudence to interpret the phrase 'sufficient specificity' in s 71(4)*(a)* of the Companies Act.

Concerns arise whether this new power given to the board of directors would stifle free debate and hinder dissent on the board, or be abused by the board of directors or used for ulterior motives. Admittedly, a director who has been unfairly removed from the board of directors has various avenues to contest his removal. Nevertheless, he would face difficulties with each of these avenues.

[131] See s 69(8)*(a)* of the Companies Act; *Kukama v Lobelo* [2012] JOL 28828 (GSJ) para 22; *Msimang NO v Katuliiba* supra note 130 para 32; *Rabinowitz v Van Graan* 2013 (5) SA 315 (GSJ).

[132] Section 162(6) of the Companies Act.

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For instance, a director would have the option to make a presentation to the board of directors to contest his removal before it votes upon the resolution. However, the director would not be entitled to make a written presentation. Moreover, his grounds for contesting his removal may not be considered by the board before the meeting to vote on his removal, and, as a result of the decision in *Pretorius*, he would not be entitled to detailed reasons for his removal, if the allegations made against him are simple and uncomplicated. To compound matters, a director does not have a statutory right to access the books and records of a company. While he may rely on the common law or s 50 of PAIA to gain such access, he would first have to satisfy the relevant stringent requirements.

A director could also apply to a court of law to review the decision to remove him from the board of directors. However, he would have to prove any suspicions of ulterior motives on a balance of probabilities. Furthermore, even if the director is able to convince the court that his removal was unfair, s 71 of the Companies Act does not specify the remedies that the court may grant. In light of the dual capacities in which an executive director holds office, it is questionable whether a court could or would order the reinstatement of a director who had been unfairly removed, or whether this would be practical. It is also unclear whether a court is empowered under s 71(5) of the Companies Act to award compensation to such a director, and if so, the basis upon which the compensation would be calculated.

A director who has been removed from office may institute a claim for damages or (other compensation) for his loss of office. While this would not result in him being reinstated to the board of directors, the fact that he has such a right would be a factor to be considered by the board of directors in considering whether to remove him from office, particularly where the damages claim would be high. However, the challenges that such a director would face are that he must have the right to claim damages (or other compensation) for his loss of office under the company's Memorandum of Incorporation or his service contract, he must not have breached the company's Memorandum of Incorporation or his service contract, and he must be able to prove his damages.

In using this new power to remove one of their own from the board of directors of a company, boards must act openly and transparently, and in the best interests of the company. It is hoped that directors do not abuse this power or use it with ulterior motives or to cover up any wrongdoing. Importantly, in light of the challenges that a director would face in contesting his removal from the board of directors, the potential for abuse of this new power must be guarded against. It remains to be seen how boards of directors will use this new power. These powers must be used sensibly, reasonably, wisely and in the best interests of the company.

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