

A Comparative Analysis of Directors' Duty of Care, Skill and Diligence in South Africa and in Australia

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First Draft - Work in Progress! Please do not quote without author's permission!

This paper, to be delivered at the 2009 Corporate Law Teachers Association, hosted by the UTS, Sydney on 1-3 February 2009, will form the basis of an article that will be published, on invitation, in a special edition of the, *Acta Juridica*, the official law review journal of the Faculty of Law, University of Cape Town in 2010. It is a special edition in memory of the late Prof. Michael Larkin, who was tragically stabbed to death in Cape Town in 2007. **Please take some time to read the tribute that the 2007 Intermediate and Final Year Law Students of the Faculty of Law, University of Cape Town, wrote after Professor Larkin's death – see end of this paper!**

I INTRODUCTION

Comparative research is fascinating, not only because it often reveals subtle differences in approaches between jurisdictions, but also because it exposes blatant difference. When these subtle difference and blatant ones are viewed together, it may bring with it a realisation that what was thought to be the same legal principles applying in different jurisdictions are in actual fact not the same at all.

In this contribution the aim is first to summarise directors' common law duty of care, skill and diligence under of the current South African law. This is followed by an analysis of the newly proposed statutory duty of care, skill and diligence contained in clause 76 of the South African Companies Bill 2008, which was adopted by Parliament on 20 October 2008. A basic overview will then be given of directors' common law and statutory duty of care and diligence in Australia. Before drawing some conclusions, the focus will also be on the differences and the similarities between the two legal systems in the area of directors' duty of care, skill and diligence.

II THE SOUTH AFRICAN LAW

(1) *Directors' common law duty of care, skill and diligence*

(a) *Delineation of the duty by academics*

The leading South African works on corporate law and directors' duties, deal with directors' duty of care, skill and diligence under slightly different headings. Cilliers and Benade¹ use the heading "duty to act with care and skill", while Henochsberg² discusses this duty under the heading "negligence". Hahlo³ and Blackman⁴ use the term "duty of care and

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¹ H S Cilliers, M L Benade, J J Henning, J J du Plessis, P A Delpont, L De Koker and JT Pretorius *Cilliers & Benade: Corporate Law* 3rd ed (2000) at 147 para 10.30-10.32.

² B Galgut (Consulting Editor) and J A Kunst, P Delpont and Q Vorster (Editors) *Henochnsberg on the Companies Act: Volume 2 Loose Leave* 5th Edition (1994 – updated until June 2008 - Service Issue 27) at 462.

³ J T Pretorius, P A Delpont, Michelle Havenga and Maria Vermaas *Hahlo's South African Company Law through the Cases - A Source Book* 6th ed (1999) at 280-284.

⁴ M S Blackman 'Companies' in *The Law of South Africa (LAWSA): Volume 4 – Part 2* (ed WA Joubert) (1996) at 232-233 para 138.

skill”, while Beuthin and Luiz⁵ simply refer to “the duty of care”. Naudé⁶ discusses this duty under the heading “sorgsaamheidsverpligtinge van direkteure”. Van Dorsten⁷ is one of the only South African commentators using the word “diligence” as part of his discussion of this duty under the heading “duty of care, skill and diligence”. In actual fact, Van Dorsten is the only South African commentator who discusses this duty under three different parts, namely “duty of care”, “duty of skill” and “diligence”. However, this apparently logical presentation provided him with considerable difficulty. Not only are the same cases and parts of the same quotes repeated under the different headings, but sentences are simply repeated verbatim under the various headings. It is also not clear at all what the actual differences are between “care” and “diligence”. The point is illustrated by Van Dorsten’s quotes from the Shorter Oxford Dictionary. He points out that “care” has been defined as “serious mental attention; concern; caution ...”,⁸ while “diligence has been defined as “careful attention, heedfulness, caution”.⁹

It is fair to say that although South African commentators use different headings to discuss this duty, there is little difference among the South African commentators when it comes to how they explain the substance of directors’ duty of care, skill and diligence. Van Dorsten, relying on *Huckerby v Elliot*,¹⁰ points out that a director is not obliged to supervise his co-directors; acquaint himself with all the details of the management of the company; or to exercise control over the day-to-day affairs of a company.¹¹ Cilliers and Benade commence their discussion of this duty by pointing out that the standards according to which the degree of care and skill is to be measured are by no means clear.¹² The reason for this is, so it is explained, that while it is to a certain extent possible to establish “care” objectively, “skill” varies from person to person. The authors then provide a practical explanation why different standards need to be applied as far as the common law duty of care and skill is concerned:

“It is not required that the directors of a steelworks must, for example, be accomplished metallurgists; a farmer, a lawyer, a medical practitioner and a pensioner may equally well serve on such a board without their lack of knowledge of steel, its qualities, production and marketing disqualifying them in any way on account of lack of skill. Nevertheless it is required of directors that they apply such skill as they do possess to the advantage of the company.”¹³

Based on the case of *Fisheries Development Corporation of SA Ltd v Jorgensen*,¹⁴ which was in turn influenced by the English cases of *In re Brazilian Rubber Plantation and*

⁵ R C Beuthin and S M Luiz *Beuthin’s Basic Company Law* 2nd ed (1992) at 224

⁶ S J Naudé *Die Regsposisie van die Maatskappydirekteur met besondere verwysing na die Interne Maatskappyverband*, LLD Thesis, UNISA, 1969 at 215.

⁷ J L van Dorsten *Rights, Powers and Duties of Directors* (1992) at 170.

⁸ J L van Dorsten *Rights, Powers and Duties of Directors* (1992) at 172.

⁹ J L van Dorsten *Rights, Powers and Duties of Directors* (1992) at 179.

¹⁰ [1970] 1 All ER 189 (QB) at 193-194.

¹¹ J L van Dorsten *Rights, Powers and Duties of Directors* (1992) at 175.

¹² H S Cilliers, M L Benade, J J Henning, J J du Plessis, P A Delpont, L De Koker and JT Pretorius *Cilliers & Benade: Corporate Law* 3rd ed (2000) at 147-148 para 10.31.

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¹⁴ 1980 (4) SA 156 (W) 165. Cf Du Plessis *Maatskappyregtelike Grondslae* 80-83; Brusser 1983 *South African Company LJ* 12.

*Estates Ltd*¹⁵ and *In re City Equitable Fire Insurance Co Ltd*,¹⁶ the authors paraphrase the concepts of “care” and “skill” as follows:

“(a) The extent of a director’s duty of care and skill depends to a considerable degree on the nature of the company’s business and on any particular obligations assumed by or assigned to him. There is a difference between the full-time or executive director, who participates in the day to day management of the company’s affairs and the non-executive director who has not undertaken any special obligation. The latter is not bound to give continuous attention to the affairs of the company. His duties are of an intermittent nature, to be performed at periodical board meetings and at any other meetings which may require his attention. He is not, however, bound to attend all such meetings, though he ought to whenever he is reasonably able to do so.

(b) A director is not required to have special business acumen or expertise, or singular ability or intelligence or even experience in the business of the company. He is, however, expected to exercise the care which can reasonably be expected of a person with his knowledge and experience. A director is not liable for mere errors of judgment.

(c) In respect of all duties that may properly be left to some other official, a director is, in the absence of specific grounds for suspicion, justified in trusting that official to perform such duties honestly. He is entitled to accept and rely on the judgment, information and advice of the management, unless there are proper reasons for questioning such. Obviously, a director exercising reasonable care would not accept information and advice blindly. He would accept it, and he would be entitled to rely on it, but he would give it due consideration and exercise his own judgment accordingly.”¹⁷

This rather long quote has been included to illustrate, as will be seen later,¹⁸ how similar the South African and Australian common law in the are of directors’ duty of care, skill and diligence was until about 1992. Since the *Fisheries Development Corporation* case, there were only a few other South African cases where directors’ duties of care, skill and diligence were mentioned. By no means did they move the South African common law, as far as directors’ duty of care, skill and diligence is concerned, strides ahead as was the case in Australia with the landmark decision of *Daniels v Anderson* in 1995.¹⁹

(b) *Unanswered questions and hidden tensions*

A comparison of the duty of care, skill and diligence as paraphrased by Cilliers and Benade and some court cases reveal that there are in actual fact several unanswered questions and quite a bit of tension in the way in which the duty of care, skill and diligence has been perceived under the South African common law. These unanswered questions and tensions are discussed under separate headings.

¹⁵ [1911] 1 Ch 425.

¹⁶ [1925] 1 Ch 407.

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¹⁹ See discussion ???>>>

(I) *Distinction between duties of executive and non executive directors*

The distinction between the duty of care and skill of “full time or executive directors” and “non executive directors” drawn by Margo J in the *Fisheries Development Corporation* case, has been heavily criticised by Goldstone JA in the case of *Howard v Herrigel*,²⁰ without specifically referring to Margo J’s specific comments in the *Fisheries Development Corporation* case:

“In my [Goldstone JA’s] opinion, it is unhelpful and even misleading to classify company directors as ‘executive’ or ‘non-executive’ for purposes of ascertaining their duties to the company or when any specific or affirmative action is required of them. No such distinction is to be found in any statute. At common law, once a person accepts an appointment as a director, he becomes a fiduciary in relation to the company and is obliged to display the utmost good faith towards the company and in his dealings on its behalf.”²¹

It could be argued that Goldstone JA only refers to directors fiduciary duties, but there are two hints that his statements also refer to directors’ duty of care, skill and diligence. First, he uses the plural (“their duties to the company”), which include all their duties (fiduciary as well as care, skill and diligence). Second, and perhaps more important, Goldstone JA expands on his statement a few lines later with the following observation:

“However, it is not helpful to say of a particular director that, because he was not an ‘executive director’, his duties were less onerous than they would have been if he were an executive director. Whether the inquiry be one in relation to negligence, reckless conduct or fraud, the legal rules are the same for all directors”.²²

It is submitted that it is safe to say that if it is currently required of any South African court to consider directors’ common law duty of care, skill and diligence, such a court will have to reconsider the distinction between the duties of executive and non-executive directors drawn in *In re City Equitable Fire Insurance Co Ltd*²³ and in *Fisheries Development Corporation of SA Ltd v Jorgensen*.²⁴

(II) *The basis of liability for a breach of directors’ duty of care, skill and diligence*

It is beyond dispute that fault (*culpa* (negligence) or *dolus* (intent))²⁵ is a requirement before a director could be held liable for a breach of his or her duty of care, skill and diligence. Thus, it has been said the basis of liability for a breach of directors’ duty of care, skill and diligence is an extension of Aquilian liability (liability under the *lex Aquilia*),²⁶ which nowadays basically means that it is the South African law of delict that forms the basis of this liability. On the other hand, no form of fault is required for a director to be in breach of his or her fiduciary duties.²⁷ Thus, it is said that the basis of directors’ liability for a breach of

²⁰ 1991 (2) SA 660 (AD).

²¹ At 678A.

²² At 678D.

²³ [1925] 1 Ch 407.

²⁴ 1980 (4) SA 156 (W) 165. Cf *Du Plessis Maatskappyregtelike Grondslae* 80-83; *Brusser* 1983 *South African Company LJ* 12.

²⁵ See *Du Plessis v Phelps* 1995 4 SA 165 (C) at 170C-D.

²⁶ *Benson v De Beers Consolidated Mines Ltd* 1988(1) 834 (NC) at 836; *Ex parte Lebowa Development Corporation Ltd* 1989 3 SA 71 (T) at 106; *Du Plessis v Phelps* 1995 4 SA 165 (C) at 170C.

²⁷ *Du Plessis v Phelps* 1995 4 SA 165 (C) at 170C-D.

fiduciary duties is *sui generis*²⁸ and that they can be in breach of their fiduciary duties even if they acted honestly and in the best interests of the company.

It is necessary to spend some time on the proposition that the basis of liability for a breach of directors' duty of care, skill and diligence is an extension of Aquilian liability. In context of the South African law it has indeed been a very unique extension of Aquilian liability. The reason is that South African courts, for historical reasons, tended to follow English precedents.²⁹ It is, therefore, very common to find South African courts and academic commentators to rely on English precedents to establish what the South African common law is. Directors' common law duties, not having been codified or even contained in South African company law legislation until 2008, is a prime example where English precedents were adopted with little adaptation.³⁰

Thus, based on English precedents, it has been accepted that directors are not liable for a breach of their duty of care, skill and diligence if they merely acted negligently. There were several English precedents where this proposition was established. One of the first indications that more than ordinary negligence was required, is the case of *Overend & Guernsey Company v Gibb*.³¹ The Lord Chancellor (Lord Hatherley) and Lord Chelmsford had no hesitation in stating that directors are only liable for a breach of their duty of care, skill and diligence if they acted with "*crassa negligentia*".³² Lindley MR, referring to *Overend & Guernsey Company v Gibb*, stated the negligence-requirement for directors like this in *Lagunas Nitrate Company v Lagunas Syndicate*³³

"The inquiry, therefore, is reduced to want of care and bona fides with a view to the interests of the nitrate company. The amount of care to be taken is difficult to define; but it is plain that directors are not liable for all the mistakes they may make, although if they had taken more care they might have avoided them: see *Overend, Gurney & Co. v. Gibb* (1872) LR 5 HL 480. Their negligence must be not the omission to take all possible care; it must be much more blameable than that: it must be in a business sense culpable or gross. I do not know how better to describe it."³⁴

Also in *Re National Bank of Wales Ltd*³⁵ Lindley MR, referring back to *Lagunas Nitrate Company v Lagunas Syndicate*, again explained the blameworthiness of directors as follows:

28 See cases and authority quoted in H S Cilliers, M L Benade, J J Henning, J J du Plessis, P A Delpont, L De Koker and JT Pretorius *Cilliers & Benade: Corporate Law* 3rd ed (2000) at 141 para 10.12 fn 24.

29 H S Cilliers, M L Benade, J J Henning, J J du Plessis, P A Delpont, L De Koker and JT Pretorius *Cilliers & Benade: Corporate Law* 3rd ed (2000) at 19 para 2.03.

30 *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W) at 165F-G: "In England certain principles have emerged from the decided cases on [a director's duty of care and skill]. There has been a relative paucity of cases in South Africa, but the essential principles of this branch of company law are the same, and the English cases provide valuable guidance." S J Naudé *Die Regsposisie van die Maatskappydirekteur met besondere verwysing na die Interne Maatskappyverband*, LLD Thesis, UNISA, 1969 puts it as follows: "Daar kan weinif twyfel bestaan dat die Engelse vonnisse waarin die 'duty of care and skill' van direkteure beliggaam is, in essensie in Suid-Afrika nagevolg sal word(at 223)" and "Die Engelse vonnisse waarin die bykans volkome subjektiewe toets vir die nalatigheid van 'n direkteur beliggaam is, word egter sonder huiwering deur Suid-Afrikaanse matskapperegskrywers as gesag gebruik, en daar kan met 'n groot mate van veiligheid snvaar word dat ons howe 'n soortgelyke houding sal inneem (at 229)".

31 [1872] LR HL 480.

32 At 487, 488, 489 493496 and 500.

33 [1899] 2 Ch 392.

34 At 435.

35 [1899] 2 Ch 629 at 672.

“In the *Lagunas Case* it was said, and we repeat it, that the amount of care to be taken is difficult to define; but it is plain that directors are not liable for all the mistakes they may make, although, if they had taken more care, they might have avoided them: see *Overend, Gurney & Co. v. Gibb*. Their negligence must be, not the omission to take all possible care; it must be much more blameable than that: it must be in a business sense culpable or gross. We do not know how better to describe it.”³⁶

Romer J, in the *City Equitable Fire Insurance Co Ltd* case, confesses that he experienced some difficulty in understanding the differences between negligence and gross negligence. He then attempts to clarify the differences by using examples, including this one:

“But if it is said that of two men one is only liable to a third person for gross negligence, and the other is liable for mere negligence, this, I think, means no more than that the duties of the two men are different. The one owes a duty to take a greater degree of care than does the other”³⁷

The one who owes a greater degree of care is the one who could be held liable for mere negligence and, that mere negligence is not enough to hold directors liable, seems to be what Romer J is trying to say:

“If, therefore, a director is only liable for gross or culpable negligence, this means that he does not owe a duty to his company, to take all possible care. It is some degree of care less than that. The care that he is bound to take has been described by Neville J. [*In re Brazilian Rubber Plantation and Estates Ltd*³⁸] as ‘reasonable care’ to be measured by the care an ordinary man might be expected to take in the circumstances on his own behalf’;³⁹ and

“It is perhaps only another way of stating the same proposition to say that directors are not liable for mere errors of judgment.”⁴⁰

That negligence alone was not enough to hold directors liable for a breach of their common law duties, was also confirmed in a leading Australian case, *Daniels v Anderson*,⁴¹ after analysing the leading English cases on the topic.⁴² The majority (Clark and Sheller JJA) referred to the concept of “negligence” as used in context of equitable remedies and concluded that “[t]he negligence spoken of was something grosser or more culpable determined by subjective rather than objective testes”.⁴³

³⁶ At 672. See also *Lagunas Nitrate Company v Lagunas Syndicate* [1899] 2 Ch 382 at 659.

³⁷ At 427.

³⁸ [1911] 1 Ch 425.

³⁹ *In re City Equitable Fire Insurance Company Limited* [1925] 1 Ch 407 at 428. It seems to have been assumed that during the late 1800s and early 1900s there was a perception, perhaps based on principles relating to trustees partnerships, that a man/woman would have been less careful in attending to his/her own affairs than when attending to the affairs of others. When one looks at several of the large corporate collapses like Enron (US), WorldCom (US), HIH (Australia), OneTel (Australia), LeisureNet (South Africa) and others, and focus on the conduct of the directors associated with these companies, it may well be argued that the values have been reversed – that directors nowadays are far more careless in attending to the affairs of others than to their own affairs.

⁴⁰ *In re City Equitable Fire Insurance Company Limited* [1925] 1 Ch 407 at 429.

⁴¹ 16 ACSR 607 (CA (NSW)).

⁴² *ibid* 657.

⁴³ *ibid*.

In short, the form of fault required *by the courts* to hold directors liable for a breach of their duty of care, skill and diligence is not the typical ordinary negligence under Aquilian liability, but something more—gross negligence or culpable negligence. Thus, it should be said that, based on the precedents, it requires some qualification when stating that the basis of liability for a breach of directors’ duty of care, skill and diligence is Aquilian in nature. It may well be Aquilian in nature, but definitely heavily influenced by English precedents.

It should, however, be pointed out that South African *academics* have been skeptical about the soundness of the influence of English precedents in this area of the law. In actual fact, the South African law of delict is quite different from what is called the tort of negligence in English-influenced jurisdictions.⁴⁴ The South African law of delict requires certain definite elements for liability: An act or deed (“handeling”); wrongfulness (“wederregtelikheid”); fault (“skuld”); damages (“skade”) and causation (“kousaliteit”). Naudé, already in 1969, points out that several academics have shown convincingly that the English “duty of care doctrine” should be rejected as far as the South African law of delict is concerned.⁴⁵ The main reason is that under the English “duty of care doctrine” the elements of “fault” and “wrongfulness” are considered simultaneously, while these elements are treated separately under the South African law of delict.⁴⁶ Naudé then considers how the various elements of the delict should be treated when the investigation is whether a director breached his duty of care, skill and diligence.⁴⁷

It should be noted that since 1969 the South courts developed and refined the principles underlying delictual liability considerably, especially as far as liability for negligent misstatements or misrepresentations are concerned causing pure economic loss. It could, therefore, be said with considerable confidence that if it is required of the South African courts to consider the liability of directors for a breach of their duty of care, skill and diligence, that it would be the principles of the modern law of delict that will be applied. This will ensure that today the influence of old English precedents will probably be viewed with skepticism by the South African Courts.⁴⁸

(III) *Standards of conduct expected of directors under the duty of care, skill and diligence*

The fact that it has been accepted in South Africa, based on the cases of *In re Brazilian Rubber Plantation and Estates Ltd*⁴⁹ and *In re City Equitable Fire Insurance Co Ltd*⁵⁰, that a director is only to exercise the care which can reasonably be expected of a person of his knowledge and experience,⁵¹ deserve some attention. Because of the subjective element

⁴⁴ See, however, D Hutchinson “Aquilian Liability II (Twentieth Century)” in *Southern Cross: Civil Law and Common Law in South Africa* (eds R Zimmermann and D Visser), (1996) 596 at 636-637 mooted the point whether it is really as different as some would like to make it out.

⁴⁵ S J Naudé *Die Regsposisie van die Maatskappydirekteur met besondere verwysing na die Interne Maatskappyverband*, LLD Thesis, UNISA, 1969 at 223-224.

⁴⁶ *ibid* 224. See also D Hutchinson “Aquilian Liability II (Twentieth Century)” in *Southern Cross: Civil Law and Common Law in South Africa* (eds R Zimmermann and D Visser), (1996) at 598, 634-635 and in particular 636; J M Burchll “The Protection of Personal Rights” in *Southern Cross: Civil Law and Common Law in South Africa* (eds R Zimmermann and D Visser), (1996) 659 at 644.

⁴⁷ S J Naudé *Die Regsposisie van die Maatskappydirekteur met besondere verwysing na die Interne Maatskappyverband*, LLD Thesis, UNISA, 1969 226-232.

⁴⁸ See further discussion under the next heading.

⁴⁹ [1911] 1 Ch 425.

⁵⁰ [1925] 1 Ch 407.

⁵¹ See *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W) at 166A.

involved in this, it has been said that in actual fact the common law standard of conduct expected from directors were remarkably low. It is, therefore, also not surprising that there has been “a relative paucity of cases in South Africa”⁵² where the main focus was the liability of directors based on a breach of their duties of care, skill and diligence. In actual fact, it was noted that by 1969,⁵³ only one company has been successful in suing its directors based on negligence. That was the case of *Niagara Ltd v Langerman*.⁵⁴

Forty years ago, Naudé defended the fact that subjective elements were taken into considerations when reviewing whether directors were in breach of their duty of care and skill. He pointed out that companies vary considerably in size and that directors with considerable different skill are appointed. Some are appointed for the prestige value only, others for their particular knowledge of the industry, for instance the professor of chemistry in a company doing business in the chemistry industry. Yet others have hardly any technical knowledge of the business, but are appointed to run the day to day business of the corporation. Based on these factual considerations, Naudé concludes that there could be no question of professional qualifications of directors.⁵⁵ Naudé then explains in detail why there was justification for adopting the English precedents which introduced subjective elements in determining whether a particular director was in breach of his duty of care and skill.⁵⁶

Naudé’s arguments seem very convincing and probably provided the correct solution for its time, especially as the community standards expected of directors were still low; the directors’ profession was still not well developed and defined; and the South African law of delict was still relatively ill-developed, especially as far as negligent misstatements or misrepresentation causing pure economic loss was concerned.

That the scene has changes considerably for directors in recent years, was strikingly illustrated by the Australian case of *Daniels v Anderson*.⁵⁷ Although the court specifically recognised the potential tension between expecting objective professional standards of all directors in all types of companies, it did not hesitate to conclude that things have changed considerably since the case of *City Equitable Fire Insurance Co Ltd*. Thus, the court held that it is the modern law of negligence that should be used to determine whether a director was in breach of his or her duty of care, skill and diligence.⁵⁸ In actual fact the court held that the modern law of negligence can cope with the potential tension between expecting objective professional standards of all directors in all types of companies.

Also in South Africa, it is beyond dispute that the scene change completely for directors since the decision of *City Equitable Fire Insurance Co Ltd* in 1925 and the South African case of *Fisheries Development Corporation of SA Ltd v Jorgensen* in 1980. The South Africa law in the areas of corporate law and corporate governance has kept pace with the latest international developments in these areas. Much development and refinement took

52 *ibid* at 165F.

53 S J Naudé *Die Regsposisie van die Maatskappydirekteur met besondere verwysing na die Interne Maatskappyverband*, LLD Thesis, UNISA, 1969 at 217.

54 1913 WLD 188.

55 S J Naudé *Die Regsposisie van die Maatskappydirekteur met besondere verwysing na die Interne Maatskappyverband*, LLD Thesis, UNISA, 1969 at 216.

56 *ibid* 230-230.

57 16 ACSR 607 (CA (NSW)).

58 at 664-665.

place, especially since the South African Companies Act 61 of 1973 came into effect in 1974. The most notable examples of considerable modernisation in South Africa in the areas of corporate law and corporate governance, are probably the adoption of the Close Corporations Act 69 of 1984; the King Reports (1994 and 2002) on Corporate Governance, which set international standards in several areas; and the South African Companies Bill 2008, which is currently one of the most advanced and modern pieces of company legislation in the world.

Thus, it is submitted that in similar vein to the Australian case of *Daniels v Anderson*, a South African court, if nowadays required to consider whether a director breached his or her common law duty of care, skill and diligence, will use modern yardsticks to determine whether a director breached his or her duty of care, skill and diligence and that will include the principles of the modern law of delict. Although there are considerable differences between the Australian tort of negligence and the South African law of delict, I can see no reason, in principle, based on policy or on practical considerations why the South African courts should not move away from the subjective standards, developed by English courts in the late 1800s and early 1900s, to determine whether a particular director was in breach of his or her duty of care, skill and diligence. The basis of liability for such a breach should be the principles of the South African law of delict. I can simply state that, after having done considerable additional research on this topic and having had considerable additional exposure to the Australian tort of negligence,⁵⁹ I have not changed my position on this issue since 1990.⁶⁰

(2) *Directors' duty of care, skill and diligence in terms of the Companies Bill 2008*

(a) *Section 43 of the Close Corporations Act 69 of 1984*

It is appropriate to commence the discussion of the proposed statutory duty of care, skill and diligence in South Africa by reference s 43 of the South African Close Corporations Act 69 of 1984. The reason is that s 43 is probably the best illustration of how directors' duty of care, skill and diligence is perceived under the South African common law. Although s 43 deals with the duty of care and skill of *members of close corporations*, it was indeed an attempt to codify the duties of members of close corporations, based primarily on *the common law duties expected of company directors*. Section 43 reads as follows:

43 Liability of members for negligence

(1) A member of a corporation shall be liable to the corporation for loss caused by his failure in the carrying on of the business of the corporation to act with the degree of care and skill that may reasonably be expected from a person of his knowledge and experience.

⁵⁹ See discussion below.

⁶⁰ JJ du Plessis *Maatskappyregtelike grongslae van die regsposisie van direkteure en besturende direkteure*, LLD Thesis, UOVS (1990) at 82-83: " 'n Probleemarea waarop daar soms gewys word, is die vraag of die verbreking van hierdie pligte [pligte to sorg en vaardigheid] objektief of subjektief beoordeel moet word. Daar word aan die hand gedoen dat dit onnodig is om breedvoerig te probeer uitspel of die beoordelingskriterium by 'n verbreking van hierdie pligte objektief of subjektief moet wees. Word aanvaar dat die grondslag van aanspreeklikheid deliktueel is, dan moet elke saak aan die hand van die beginsels van die Suid-Afrikaanse deliktereg beoordeel word. Alvorens die direkteur aanspreeklikheid kan opdoen vir die skending van hierdie pligte, sal die hof immers eers moet vra of sy optrede onregmatig was en of hy met die nodige skuld opgetree het. Die wyse waarop hierdie twee elemente van die onregmatige daad beoordeel word, vervang die nodigheid daarvan om in maatskappyregtelike verband te probeer vasstel of hierdie pligte objektief of subjektief beoordeel moet word. In beginsel is daar nie eiesoortige deliktuele probleme voorhande as die skuld van direkteure vasgestel moet word nie. Die vraag na hul skuld behoort bloot gesien te word as 'n spesies van die probleem wat opduik ter bepaling van die skuld van deskundiges."

(2) Liability referred to in subsection (1) shall not be incurred if the relevant conduct was preceded or followed by the written approval of all the members where such members were or are cognisant of all the material facts.

Sub-section (2) is clearly aimed at the prior (“preceded ... written approval”) or ex post facto approval (“followed by the written approval”) of a breach of this duty. The qualification is that in both instances the members must have been cognisant of all the material facts before they could approve or condone a breach of this duty. As mentioned, s 43 of the Close Corporations Act 69 of 1984 in actual fact neatly captures directors’ common law duty of care, skill and diligence as perceived in South Africa. There is also little doubt that company law cases will be used in interpreting the standards expected of members of close corporations under s 43.⁶¹ This, unfortunately, means that the influence of older English cases as discussed above will remain dominant even in the case of the codified duties of members of close corporations. This is particularly so because the subjective element of the standard of care and skill has specifically been maintained in s 43(1) — “the degree of care and skill that may reasonably be expected *from a person of his knowledge and experience*” (emphasis added).

It is submitted that it would have been better if the liability of members of close for corporations for “negligence” was based squarely on the modern law of delict, but with some statutory provision, similar to the Australian provision (s 180(1) of the Australian Corporations Act 2001), to ensure that a breach of this duty is measured objectively, but taking into consideration circumstances relating to other members occupying a similar position as the position of the member who allegedly breached his or her duty of care, skill and diligence (similar to s 180(1)(b) of the Australian Corporations Act 2001). Also, it is appropriate to measure a breach of the duty against persons having the same responsibilities within the corporation as the member who allegedly breached his or her duty of care, skill and diligence (again similar to s 180(1)(b) of the Australian Corporations Act 2001. In actual fact, s 180(1)(a) also requires that the standard of conduct of a director in breach of his or her duty of care and diligence, should be judged as if the directors was “a director or officer of a corporation in the corporation’s circumstances” (s 180(1)(a) of the Australian Corporations Act 2001). It is submitted that this requirement is unnecessary. It is inconceivable that a court, in judging the breach of a directors’ duty of care and diligence will take it completely out of context and judge the duty of care and diligence of a director in a small private company in context of a large public company or *vice versa*. It goes without saying that courts will judge the breach in context of a “reasonable person” in the particular company’s circumstances.

(b) *Clause 76 of the Companies Bill 2008*

(I) *Comparable other statutory provisions and overview clause 76*

There has never been a general attempt in South Africa to codify directors’ common law duties or to express them in company law legislation. These duties, similar to the UK until the UK Companies Act of 2006, have always been seen as developed by the courts and, as was pointed out above, heavily influenced by English precedents. However, as mentioned in the previous part, s 43 of the Close Corporations Act 69 of 1984 was an attempt to extract the common law company principles, as far as the duty of care skill and diligence was

⁶¹ See and compare PM Meskin (assisted by JA Kunst) *Henochsberg on the Close Corporations Act: Volume 3* (1997) Com-111 para 43.2 and ML Benade, JJ Henning, JJ du Plessis, PA Delpont, L De Koker and JT Pretorius *Entrepreneurial Law*, 4th Edition (2008) 325 paras 28.05-28.07.

concerned, and state them in the Close Corporations Act 69 of 1984. There was in actual fact some consideration given to simply replace “member of a close corporation” with “director of a company” in s 43 of the Close Corporations Act 69 of 1984 and incorporated such a provision in the new company law legislation, which is now the Companies Bill of 2008.

Apart from section 43 of the Close Corporations Act 61 of 1984, there is another example of directors’ duties contained in South African legislation. This is in the area of banking law. All South African banks fall under the Banks Act 94 of 1990 and, in terms of s 60 of the Banking Act 61 of 1990, directors’ statutory duties are expressed as follows:

“60 Directors of bank or controlling company

(1) Each director, chief executive officer and executive officer of a bank owes a fiduciary duty and a duty of care and skill to the bank of which such a person is a director, chief executive officer or executive officer.

(1A) Each director, chief executive officer and executive officer of a bank owes a duty towards the bank to-

- (a) act bona fide for the benefit of the bank;
- (b) avoid any conflict between the bank's interests and the interests of such a director, chief executive officer or executive officer, as the case may be;
- (c) possess and maintain the knowledge and skill that may reasonably be expected of a person holding a similar appointment and carrying out similar functions as are carried out by the director, chief executive officer or executive officer of that bank; and
- (d) exercise such care in the carrying out of his or her functions in relation to that bank as may reasonably be expected of a diligent person who holds the same appointment under similar circumstances, and who possesses both the knowledge and skill mentioned in paragraph (c) and any such additional knowledge and skill as the director, chief executive officer or executive officer in question may have.

It will be clear that it is s 60(1A)(c) and (d) that deal with bank directors’ duty of care, skill and diligence. During the South African corporate law reform process, there was also consideration given to simply include these provisions into the new South African company legislation.

Although there were long discussions, and directors’ statutory duties formulated in different ways in several initial drafts of the Companies Bill, clause 76 of the Companies Bill 2008 is the current clause dealing with directors’ statutory duties:

76. (1) In this section, “**director**” includes an alternate director, and—

- (a) a prescribed officer; or
- (b) a person who is a member of a committee of a board of a company, or of the audit committee of a company, irrespective of whether or not the person is also a member of the company’s board.

(2) A director of a company must—

- (a) not use the position of director, or any information obtained while acting in the capacity of a director—
 - (i) to gain an advantage for the director, or for another person other than the company or a wholly-owned subsidiary of the company; or

- (ii) to knowingly cause harm to the company or a subsidiary of the company; and
- (b) communicate to the board at the earliest practicable opportunity any information that comes to the director's attention, unless the director—
 - (i) reasonably believes that the information is—
 - (aa) immaterial to the company; or
 - (bb) generally available to the public, or known to the other directors; or
 - (ii) is bound not to disclose that information by a legal or ethical obligation of confidentiality.

- (3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director—
- (a) in good faith and for a proper purpose;
 - (b) in the best interests of the company; and
 - (c) with the degree of care, skill and diligence that may reasonably be expected of a person—
 - (i) carrying out the same functions in relation to the company as those carried out by that director; and
 - (ii) having the general knowledge, skill and experience of that director.

It is clear “**Prescribed officer**” is defined as “the holder of an office, within a company, that has been designated by the Minister in terms of section 66(11). It will be clear that in terms of clause 76(1)(b) even non-directors, who serve on board committees, are brought within the ambit of the statutory duties contained in clause 76(2) and (3).

Clause 76(2)(i)(a) contain the duties that are normally describe as directors’ fiduciary duties to prevent a conflict of his duty to the company and his personal interest, as well as the general principles expressed in *Regal (Hastings) Ltd v Gulliver*⁶² that a director may not abuse misuse his position as director or information obtained in his capacity as directors, for instance compete with the company (corporate opportunities) or use inside information to gain a personal advantage or an advantage for any other party person. It was thought to make sure that this restrictive duty should not, in a very technical sense, deter the director to seek advantages for his or her own company, thus the inclusion of the words “other than the company” in clause 76(2)(i). Another qualification is made, namely were the director use his position or any information obtained while acting in the capacity of a director “to gain an advantage for ... a wholly owned subsidiary of the company”. In other jurisdiction, this exception is normally more restricted.⁶³

⁶² [1942] 1 All ER 378 (HL).

⁶³ See, for instance, s 187 of the Australian Corporations Act 2001:
187 Directors of wholly-owned subsidiaries

A director of a corporation that is a wholly-owned subsidiary of a body corporate is taken to act in good faith in the best interests of the subsidiary if:

- (a) the constitution of the subsidiary expressly authorises the director to act in the best interests of the holding company; and
- (b) the director acts in good faith in the best interests of the holding company; and
- (c) the subsidiary is not insolvent at the time the director acts and does not become insolvent because of the director's act.

(II) *General noteworthy aspects regarding clause 76(3)(c) — directors’ duty of “care, skill and diligence”*

It is clause 76(3)(c) that deals with directors’ duty of care skill and diligence. There are several quite interesting aspects about clause 76(3)(c) that should be noted. A few general comments will first be made, before the focus turns to subjective elements of clause 76(3) in particular. As far as general noteworthy aspects are concerned, *first*, it should be noted that the word “diligence”, hardly ever used by South African commentators or South African courts, are also included in clause 76(3)(c). There is little doubt that this has been derived from the Australian legislation — s 180(1) of the Australian Corporations Act 2001.

Second, and linked to the previous point, the standards expected of directors are not standards of “care and diligence” only (it will be accepted that the “care and diligence” should be seen as a term, rather than trying to distinguish between “care” and “diligence” — see discussion above), it also includes a standard of “skill”. The “skills”-part of this duty was removed in Australia from the moment that this duty was expressed in a statutory provision by 1958.⁶⁴

Three, clause 76(3) links the duty of care, skill and diligence to situations where directors act “in the capacity of director” and when it is required that he or she “must exercise the powers and perform the functions of director”. It is most likely that directors will in future try to argue that for whatever breach they are sued under clause 76(3), they did not act in that capacity or exercising the powers or performed the functions of director when the alleged breach occurred. Also, because clause 76 also applies to what has traditionally been dealt with under directors’ fiduciary duties under South African law (see clause 76(3)(a) and (b)), it could be expected that in future this section will be interpreted in context of the moot point whether or not directors only owe their duties to the company when actin “as agents”.⁶⁵ Second, it deviates from the wording used by South African and English cases by using “general knowledge” rather than just “knowledge”. It is not clear what the aims are to include “general”, except for trying to give it a more objective flavour. Third, some element of objective standard of review is contained in clause 76(3)(c)(i) by judging a breach against the standards of a person “carrying out the same functions in relation to the company as those carried out by that director”.

(III) *Subjective elements of clause 76(3)(c)*

The most noticeable aspect of clause 76(3)(c) is probably that it did not objectify directors’ duty of care, skill and diligence completely. The degree of care, skill and diligence that is expected of directors under this clause is not that of a “reasonable person”, but what could “reasonably expected of a person ... *having the general knowledge, skill and experience of that director*”. It will be recalled that the common law requirement was that a director should “*exercise the care which can reasonably be expected of a person with his knowledge and experience*” (emphasis added).⁶⁶ That requirement is also captured in s 43(1) of the Close Corporations Act 69 of 1984 — “the degree of care and skill that may reasonably be expected from a person of his knowledge and experience”. Clause 76(3)(c) of the South African

⁶⁴ See *Daniels v Anderson* 16 ACSR 607(CA(NSW)) at 660.

⁶⁵ See, *Sibex Construction (SA) (Pty) Ltd v Injectaseal CC* 1988 2 SA 54 (T) at 64F-65F and 66J-67A; *Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd* 1981 2 SA 173 (T) at 198D-199C; *Robinson v Randfontein Estate Gold Mining Co Ltd* 1921 AD 168 at 216.

⁶⁶ *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W) at 166A-B.

Companies Bill 2008 is, therefore, clearly on a different path than s 180(1) of the Australian Corporations Act 2001, but let us consider the implications of this.

It is submitted that nothing should be made of the fact that the words “reasonable person” are not used, but “reasonably be expected of a person”, except that clause 76(3)(c)(ii) introduces subjective elements, making it impossible to have used the “reasonable person”-concept in that subsection. It is submitted that basically this clause provides that there is a reasonable expectation that directors should act with the “general knowledge, skill and experience” of persons with comparable “general knowledge, skill and experience”. In other words, although at first glance it seems silly to expect a person to act differently than what one would expect of him or her (taking into consideration his or her “general knowledge, skill and experience), there is a very useful aim in the way the section was drafted. The standard of care, skill and diligence of a South African director will indeed not be reviewed completely objectively, but the court will first have to determine what the expectations are of directors “carrying out the same functions in relation to the company as those carried out by that director (director whose conduct is scrutinised)” (s 76(3)(c)(i)). Then, the court will also have to make a value judgment as to how other directors, with “the general knowledge, skill and experience of that director (director whose conduct is scrutinised)” (s 76(3)(c)(ii)), would have conducted themselves. Thus, the intention of the legislature is simply to ensure that apples are compared with apples and, putting all the apples, as far as that is theoretically possible, in the same hypothetical situation comparable to the facts of the particular case!

(3) Common law and statutory protection for directors as far as their duty of care, skill and diligence is concerned

To be completed if time and space permit!

III THE AUSTRALIAN LAW

(1) Directors’ common law duties and duties in equity

As mentioned above, the way in which the South African courts perceived directors’ duty of care, skill and diligence roughly accords with the prevailing views in Australia up to about 1992. This statement is based on the comments made by Rogers CJ in the 1992 case of *AWA v Daniels*.⁶⁷ In dealing with the duty of care and diligence of non-executive directors, Rogers J made several statements which were clearly influenced by English precedents of the late 1800s and early 1900s.⁶⁸ It is unnecessary to analyse these statements in detail, because they caused the Court of Appeal of the Supreme Court of New South Wales considerable concern, requiring of them to paraphrase what Rogers CJ said in *AWA v Daniels*. For current purposes and for purposes of comparing the state of the law regarding directors’ duty of care, skill and diligence in South Africa and Australia, it is appropriate to include this rather long quote from *Daniels v Anderson*:⁶⁹

“A matter of particular significance in these appeals is the extent to which directors are justified in trusting and relying upon officers of the company. Rogers J said that a director is justified in trusting such officers to perform all duties that, having regard to the exigencies of business, the intelligent devolution of labour and the articles of

⁶⁷ (1992) 7 ACSR 759.

⁶⁸ *ibid* 864 et seq, 869 et seq.

⁶⁹ 16 ACSR 607(CA (NSW)).

association, may properly be left to them. He said that a director is entitled to rely without verification on the judgment, information and advice of the officers so entrusted and on management to go through relevant financial and other information of the corporation and draw to the board's attention any matter requiring their consideration. The business of a corporation could not go on if directors could not trust those who are put into a position of trust for the express purpose of attending to details of management. Reliance would only be unreasonable where the director was aware of circumstances of such a character, so plain, so manifest and so simple of appreciation that no person, with any degree of prudence, acting on his behalf, would have relied on the particular judgment, information and advice of the officers. A non-executive director does not have to turn him or herself into an auditor, managing director, chairman or other officer to find out whether management is deceiving him or her. These are the words uttered in 1872 by Lord Hatherly LC in *Overend & Gurney Co v Gibb* (1872) LR 5 HL 480 at 487 in describing *crassa negligentia*."

These sentiment of Rogers CJ were then rejected by the court in *Daniels v Anderson* by stating in no uncertain terms that in the court's "respectful opinion it does not accurately state the extent of the duty of directors whether non-executive or not in modern company law."⁷⁰ This rejection by the Court of Appeal of the New South Wales Supreme Court, provides an excellent opportunity to discuss the case of *Daniels v Anderson* in greater detail

It is no overstatement to say that *Daniels v Anderson* represents the pinnacle in Australia (and probably also in other jurisdictions influenced by English law!) of the development of directors' duty of care, skill and diligence that only started to emerge in greater detail in about 1869 with the case of *Turquand v Marshall*.⁷¹

Daniels v Anderson is rather difficult to digest without a good understanding of some of the unique features of the Australian law. Different from the South African law where the distinction between common law remedies and equitable remedies are insignificant, this distinction still plays an important role in the Australian law.⁷² What South African commentators will simply call directors' common law duties (the duty of care and skill as well as directors' fiduciary duties), will be divided into common law duties (the duty of care and diligence) and duties in equity (fiduciary duties). This distinction is still prominent in the Australian Corporations Act 2001.⁷³ In actual fact, an important part of the *Daniels v Anderson* case⁷⁴ deal with the liability of directors for negligence and, in particular, the consequences of the fact that the cause of action was not based a breach of any equitable or fiduciary duty, but a claim for common law damages, in particular the tort of negligence.

⁷⁰ *Daniels v Anderson* 16 ACSR 607(CA(NSW)) at 665.

⁷¹ (1869) LR 4 Ch App 376. Before this, the general "duty of care, skill and diligence" expected of office-bearers will probably have to be traced back through the law of partnerships and the law of trusts or even municipal boroughs, trade guilds and merchants associations.

⁷² RP Austin and IM Ramsay, *Ford's Principles of Corporations Law*, 13th edition, 2007 at 398-402, para 8.320.

⁷³ For instance, the term "general law" is defined as "the principles and rules of the *common law and equity*"; and in s 132(2) it is provided that "[d]espite any rule of law or equity ...". As far as directors' duties in particular is concerned, the distinction is prominent. Section 180(2), containing the so-called business judgment rule, provides that "[a] director or other officer of a corporation who makes a business judgment is taken to meet the requirements of subsection (1), *and their equivalent duties at common law and in equity*, in respect of the judgment if they ...", and in the concluding sentence to s 185 it is provided that s 185 "does not apply to subsections 180(2) and (3) to the extent to which they operate on *the duties at common law and in equity* that are equivalent to the requirements of subsection 180(1)" (emphasis added).

⁷⁴ 16 ACSR 607(CA(NSW)) at 652-668.

There are several very technical aspects dealt with in the case, but in essence the majority (hereafter referred to as “the court”)⁷⁵ of the Supreme Court of New South Wales held that the general law relating to the tort of negligence was an appropriate basis for the claim of common law damages against negligent directors. This is probably the most important and also the most unique part of the case, as there has never been any other case in any other traditional common law jurisdiction where the tort of negligence has been identified so prominently as the basis of liability for directors in breach of their duty of care, skill and diligence. It is worth quoting all the parts where the court identified the tort of negligence as the basis of directors duty of care, skill and diligence, or, as it should probably be referred to now, to determine whether a director owed a duty of care and whether that duty was breached:

“The courts have recognised that directors must be allowed to make business judgments and business decisions in a spirit of enterprise untrammelled by the concerns of conservative investment trustees Great risks may be taken in the hope of commensurate rewards. If such ventures fail, how is the undertaking of it to be judged against an allegation of negligence by the entrepreneur? In our opinion the concept of negligence which depends ultimately ‘upon a general public sentiment of moral wrongdoing for which offenders must pay (*Donohue v Stevenson* [1932] AC 562 at 580) can adapt to measure appropriately in the given case whether the acts or omissions of an entrepreneur are negligent.”⁷⁶

“We are of the opinion that a director owes to the company a duty to take reasonable care in the performance of the office. As the law of negligence has developed no satisfactory policy ground survives for excluding directors from the general requirement that they exercise reasonable care in the performance of their office. A directors’ fiduciary obligations do not preclude the common law duty of care.”⁷⁷

“The duty is a common law duty to take reasonable care owed severally by persons who are fiduciary agents bound to exercise the powers conferred upon them for private purposes or for any purpose foreign to the power and placed, in the words of Ford and Austin, *Principles of Corporations Law*, 6th ed at 429, at the apex of the structure of direction and management Breach of the duty will found an action for negligence at the suit of the company. Negligent directors are tortfeasors”⁷⁸

The court adopted the general principles of the tort of negligence and the duty of care after drawing the attention to three very important things. *First*, there were historic reasons why directors’ duty of care, skill and diligence were viewed in a particular manner by the English courts of the late 1800s and early 1900s. Referring to the article of Jennifer Hill,⁷⁹ the court make the following observation:

“The nature and extent of directors’ liability for their acts and omissions developed as the body of corporate evolved from the unincorporated joint stock company regulated by a deed of settlement and was influenced by the partnership theory of corporation

⁷⁵ Clarke and Sheller JJA. Powell JA dissented based on his view that the more traditional approach should be adopted.

⁷⁶ *Daniels v Anderson* 16 ACSR 607(CA(NSW)) at 664-665.

⁷⁷ *ibid* at 668.

⁷⁸ *ibid*.

⁷⁹ Jennifer Hill, “The Liability of passive directors: *Morley v Statewide Tobacco Services Ltd*, (1992) 14 *Syd LR* 504.

whereunder shareholders were ultimately responsible for unwise appointment of directors.”⁸⁰

Thus, the duty of care, skill and diligence expected of directors were “remarkably low ... [h]owever ridiculous and absurd the conduct of the directors, it was the company’s misfortune that such unwise directors were chosen.”⁸¹ It should, however, also be realised that apart from these reasons mentioned by the court, there were several other reasons why the courts were reluctant to scrutinise the particular acts of directors: directors were expected to take risks and the are dealing with uncertainties, which would be compromised if too high standards of care were expected of directors;⁸² courts are ill-equipped to second-guess directors’ business decisions, which resulted in a rather ill-developed “business judgment” in jurisdictions like the UK, Australia and South Africa; the internal management of the company is one that companies can arrange as they wish fit and courts should be reluctant to interfere with internal company matters etc.

The second thing the court took into consideration in embracing the tort of negligence as the basis of liability for a breach of a director’s duty of care, skill and diligence, was that “the law about the duty of directors” developed considerably since the decision in *Re City Equitable Fire Insurance Co.*⁸³ The court then, in roughly seven pages,⁸⁴ painstakingly quote from modern cases before reaching the conclusion that the tort of negligence and the modern concept of a duty of care now form an acceptable basis of liability for directors’ breach of their duty of care.⁸⁵ *The third thing* the court mentions, is that also the law of negligence has developed considerably in the seventy years (*Daniel’s* case was decided in 1995) since the decision in *Re City Equitable Fire Insurance Co.*⁸⁶

I can see no reason, in principle, based on policy or on practical considerations why these three reasons should not be used by any South African court to accept the principles of the law of delict as the basis for the liability of a breach of directors’ common law duty of care, skill and diligence. This is so irrespective of the fact that there are considerable differences in *the approach* to the South African law of delict, in particular as far as the elements of “fault” and “wrongfulness is concerned, and the Australian tort of negligence, in particular as far a the duty of care concept is concerned.⁸⁷ As far the *outcomes* of adopting the

⁸⁰ *Daniels v Anderson* 16 ACSR 607(CA(NSW)) at 657.

⁸¹ *ibid* 658-659, which is in actual fact a reference to what was said in *Turquand v Marshall* (1869) LR 4 Ch App 376 at 386: “It was within the powers of the deed to lend to a brother director, and however foolish the loan might have been, so long as it was within the powers of the directors, the Court could not interfere and make them liable ... Whatever may have been the amount lent to anybody, however ridiculous and absurd their conduct might seem, it was the misfortune of the company that they chose such unwise directors; but as long as they kept within the powers of their deed, the Court could not interfere with the discretion exercised by them.” The Cooney Report (Senate Standing Committee on Legal and Constitutional Affairs, *Company Directors’ Duties—Report on the Social and Fiduciary Duties and Obligations of Company Directors* (Cooney Report), 1989 at 20 para 3.3 fn 2, also cite the following cases for similar sentiments: “*Re New Mashonaland Exploration Co* [1892] 3 Ch D 577 at 585 per Vaughan Williams J; *Re Forest of Dean Coal Mining Co* (1878) 10 Ch D 450 at 453 per Jessel MR; *Re Faure Electric Accumulator Co* (1888) 40 Ch D 141 at 152 Per Kay J.

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⁸³ *ibid* at 661.

⁸⁴ *ibid* at 661-667,

⁸⁵ *ibid* at 668.

⁸⁶ *ibid* at 661.

⁸⁷ D Hutchinson “Aquilian Liability II (Twentieth Century)” in *Southern Cross: Civil Law and Common Law in South Africa* (eds R Zimmermann and D Visser), (1996) 596 at explains as follows: “The mist vociferous critic of the duty concept was Price, who conducted a long and acrimonious campaign to rid our law (the South African Law) of this ‘alien and disturbing’ element. Echoing the view of Buckland, who considered the concept ‘an unnecessary fifth wheel on the coach, incapable of sound analysis and possibly

different approaches are concerned, I would be very surprised if there will be any significant difference in outcome between the two jurisdictions. To put it differently, I think the outcome of *Daniels v Anderson* would have been exactly the same if the general principles of the law of delict was applied — although the processes differ, they aim at solving the same problem and, depending on which process one is more familiar with, one might prefer the one or the other.⁸⁸ Personally I find the South African law of delict to be more systematic and more scientific. There also seems to be, probably because of the clearer guidance on the elements of “negligence” and “wrongfulness” by South African courts, fewer conflicting precedents under the South African law of torts than under the Australian tort of negligence.

It is submitted that the court in *Daniels v Anderson* did not exclude the possibility that in future the liability of Australian company directors could still be based on the traditional, English influenced concept of gross or culpable negligence determined by subjective elements. Also, the court did not hold that equitable remedies for a breach of directors’ fiduciary duties will not be available to shareholders. However, the tort of negligence would be a much easier cause of action to rely on than the English influenced common law remedy for a breach of directors’ duty of care, skill and diligence, based on the concept of gross or culpable negligence and determined by subjective elements. Thus, it is highly probable that in future Australian companies will rely on the tort of negligence to sue their directors in breach of their duty of care if they choose to rely on non-statutory remedies. However, it is no secret that predominantly it is the statutory duties of Australian directors that are enforced, especially because of the dominant role the primary corporate regulator, the Australian Securities and Investments Commission (ASIC), plays in instituting action against directors for a breach of their statutory duties.⁸⁹ This brings us to a discussion of directors’ duty of care and skill in terms of the Australian Corporations Act 2001.

(2) Directors’ statutory duty of care and diligence

(a) Has directors’ duty of care and diligence been Codified⁹⁰ completely in Australia?

It is quite important to consider this question, as it determines whether the giant-step taken by *Daniels v Anderson* as far as directors’ duty of care is concerned, has any practical application. Section 180(1) of the Australian Corporations Act 2001 provides as follows:

productive of injustice’, Price argued that it was not only confusing and ambiguous but also tautologous, in that it merely repeated the foreseeability test for fault”.

⁸⁸ See again D Hutchinson “Aquilian Liability II (Twentieth Century)” in *Southern Cross: Civil Law and Common Law in South Africa* (eds R Zimmermann and D Visser), (1996) 596 at 636-637.

⁸⁹ Dee JJ du Plessis, J McConville and M Bagaric, *Principles of Contemporary Corporate Governance* (2005) at 259-260.

⁹⁰ Under “Codification”, I mean that it is only the statutory provision that will apply and that the “general law” (defined in terms of s 9 of the Australian Corporations Act 2001, as “the principles and rules of the common law and equity”) will no longer apply. An example of Codification under the Australian Corporations Act 2001, is the rule in *Foss v Harbottle* – s 236 of the Act deals with the issue how proceedings are brought on behalf of a company and how companies can intervene in proceedings. S 236(3) provides a clear example of codification of this area, by providing that “[t]he right of a person at general law (see again definition above) to bring, or intervene in, proceedings on behalf of a company is abolished” (emphasis added). In other words, the rule in *Foss v Harbottle* has no place in Australian corporations law any longer – the law has been Codified!

180 Care and diligence—civil obligation only

Care and diligence—directors and other officers

- (1) A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:
 - (a) were a director or officer of a corporation in the corporation's circumstances; and
 - (b) occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.

Note: This subsection is a civil penalty provision (see section 1317E).

Section 185 of the Australian Corporations Act 2001 provides as follows:

185 Interaction of sections 180 to 184 with other laws etc.

Sections 180 to 184:

- (a) have effect in addition to, and not in derogation of, any rule of law relating to the duty or liability of a person because of their office or employment in relation to a corporation; and
- (b) do not prevent the commencement of civil proceedings for a breach of a duty or in respect of a liability referred to in paragraph (a).

I think that the only safe thing to conclude from s 185 is that it clearly states that s 180(1) – directors' statutory duty of care and diligence – is not a codification of directors' duty of care and diligence. It is, however, far more difficult to determine to what extent the common law business judgment rule has been codified. The difficulty arises from the wording of the concluding sentence of s 185, reading as follows:

“This section (s 185) does not apply to subsections 180(2) and (3) to the extent to which they operate on the duties at common law and in equity that are equivalent to the requirements of subsection 180(1).”

The Australian business judgment rule is contained in s 180(2) and (3). In other words, the concluding sentence in s 185 predominantly excludes the application of the main part of s 185 as far as the business judgment rule (subsection 180(2) and (3)) is concerned. The difficulty to comprehend the actual meaning of this exclusion comes in sharp focus when it is realised that there are *two separate qualifications* contained in the concluding sentence of s 185 as far as the general application of s 185 is concerned. *First*, the concluding sentence of s 185 provides that s 185 does not apply to subsection 180(2) and (3). However, *the second qualification* is that it only does not apply “*to the extent to which*” the two subsections (ss 180(2) and (3)) “operate on the duties at common law and in equity”.

One way of trying to solve the riddle, is to try and interject or interpolate the qualifications in the concluding sentence of s 185 into the main parts of s 185, namely s 185(a) and (b). This process of interjection or interpolation reveals that the last sentence of s 185 in actual fact provides that s 180(2) and (3) “[*does not*] have effect in addition to, and [*is*] in derogation of, any rule of law relating to the duty or liability of a person because of their office or employment in relation to a corporation” (s 185(a)). It becomes quite ridiculous to also put s 185(b) in the negative, but it illustrates the difficulty in interpreting the concluding

sentence of s 185: it reveals that s 180(2) and (3) in actual fact “[*does prevent*] the commencement of civil proceedings for a breach of a duty or in respect of a liability referred to in paragraph (a)” (s 185(b)). For the sake of convenience and the absurdity involved in attempting to reconcile the last sentence of s 185 with s 185(b), it will be accepted that there was simply a terrible drafting error involved in trying to link the last sentence in s 185 with s 185(b). After all, neither s 180(2) or (3), nor s 185(a) deal with the “commencement” of civil action — s 180(2) and (3) deals with the business judgment rule, which is supposed to be a protection against liability of directors and s 185(a) only aims at telling us that the statutory duties in ss 180 to 184 is no codification. In short, based on an absurd outcome, it will for current purposes simply be assumed that it was an unintended drafting error by the legislature to try and link the concluding sentence in s 185 with s 185(b).

However, there seems to be an actual purpose in the link between the concluding sentence in s 185 and s 185(a). In the first part of the concluding sentence of s 185, the legislature basically tells us that the statutory business judgment rule (s 180(1) and (2)) has been codified. Why, because the legislature tells us that as far as a very tiny part of the statutory provision in sections 180-184 is concerned, i.e. ss 180(2) and (3) (the business judgment rule), it *does not* have effect in addition to and it *is* in derogation of any related rule of law.

If the legislature stopped there it would have been a fine sort of fine, although it is not easy at all for me to foresee the actual implications of this provision. However, it is the second qualification that causes even more confusion. The statutory business judgment rule will only apply “to the extent to which [it operates] on the duties at common law and in equity that are equivalent to the requirements of [directors’ statutory duty of care and diligence]”. The question then begs “to which extent will the statutory business judgment rule *not* apply to directors’ duties at common law and in equity that are *not* equivalent to the requirements of directors’ statutory duty of care and diligence? Would it be possible for a company to allege that a director who otherwise could rely on the protection of the business judgment rule cannot rely on its protection because the extent of the statutory duty of care and diligence is wider or narrower than this duty under the common law or in equity?”

Several of the Australian corporations law texts do not even mention s 185, while others simply refer to the main part of section 185, but not to the concluding sentence in s 185. There are only two texts that could be found, dealing with the concluding sentence of s 185, but neither provides any clear explanation of the aims or scope of the concluding sentence in s 185. Hinchy and McDermott⁹¹ simply states that “[s]ection 185 further states that the section does not apply to s 18(2) and (3) to the extent to which they operate on the duties at common law and in equity that are equivalent to the requirements of s 180(1)”. In other words, simply repeating the wording of the concluding sentence of s 185, without any further explanation or clarification what it means.

Austin, Ford and Ramsay only explain that “s 185 provides that the operation of the business judgment rule enunciated in s 180(2) and (3) is *not confined* to the statutory duty of care” (emphasis added).⁹² Not only does this not refer to the qualification, “to the extent to which they (ss 180(2) and (3)) operate on the duties at common law and in equity that are equivalent to the requirements of subsection 180(1) [which contains the statutory duty of care]”, but the authors’ statement seems to be based on a misinterpretation of the concluding

⁹¹ R Hinchy and P McDermott, *Company Law*, 2nd Edition, 2006 at 165.

⁹² RP Austin, HAJ Ford and IM Ramsay, *Company Directors: Principles of Law and Corporate Governance*, 2005 at 683 para 18.6.

sentence of s 185. It is after all stated very clearly in the “Note” to s 180(2) that the business judgment rule as contained in s 180(2),

“only operates in relation to duties under this section and their equivalent duties at common law or in equity (including the duty of care that arises under the common law principles governing liability for negligence)—it does not operate in relation to duties under any other provision of this Act or under any other laws.”

That seems to indicate that the protection of the business judgment rule is indeed, different from what Austin, Ford and Ramsay state, *confined* to protection against a breach of directors’ statutory duty of care and diligence and any duty comparable to that statutory duty.⁹³ It is submitted that the concluding sentence of section 185 does not only lead to an absurdity, but it is impossible to determine what its aims or its scope are.

(b) *Development and refinement of directors’ statutory duty of care and diligence in Australia*

It is remarkable to note that the predecessor of the current s 180(1) (directors’ duty of care and diligence) was already incorporated in the Victorian Companies Act in 1958 and in Tasmanian law in 1959.⁹⁴ It is surely true that at that stage there was no equivalent statutory provision in any other legislation relating to companies in the English speaking world.⁹⁵

Section 107 of the Victorian Companies Act 1958 provided as follows:

“107(1) A director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office.

(2) Any officer of a company shall not make use of any information acquired by virtue of his position as an officer to gain an improper advantage for himself or to cause detriment to the comp[any].

(3) Any officer who commits a breach of the foregoing provisions of this section shall be guilty of an offence against this Act and shall be liable to a penalty of not more than Five hundred pounds and shall in addition be liable to the company for any profit made by him or for any damage suffered by the company as a result of the breach of any such provision.

(4) Nothing in this section shall prejudice the operation of any other enactment or rule of law relating to the duty or liability of directors or officers of a company.”

This provision became s 124 of the Australian Uniform Companies Acts 1961, with only one significant addition. Instead of referring only to “gain an improper advantage” in s 107(1), s 124(1) added “directly or indirectly” – “gain directly or indirectly an improper advantage”. Section 124(4) was drafted more elegantly, to read as follows:

“124(4) This section is in addition to and not in derogation of any other enactment or rule of law relating to the duty or liability of directors or officers of a company.”

⁹³ The part included in this note including “the duty of care that arises under the common law principles governing liability for negligence” is clearly an attempt to ensure that the business judgment rule may in principle also be available to directors if sued under the tort of negligence explained in *Daniels v Anderson* 16 ACSR 607(CA(NSW)), in contrast with the more traditional common law duty of care, skill and diligence developed primarily by older English cases as explained above.

⁹⁴ Cooney Report 24 para 3.15.

⁹⁵ *Daniels v Anderson* 16 ACSR 607(CA(NSW)) at 660.

It will be noticed that s 124(4) reflects what is currently contained in s 185(a) of the Australian Corporations Act 2001, but without any qualifications and in a much more direct and straight forward way.

The general excitement of having introduced some specific statutory duties, that created the impression of setting objective standard for directors long before any other English-speaking country did so, was short-lived because of a particular interpretation of the statutory duty of “reasonable diligence” contained in s 107(1) of the Victorian Companies Act 1958 by the Full Court of the Victorian Supreme Court in the case of *Byrne v Baker*.⁹⁶ As s 107(1) of the Victorian Companies Act 1958 and s 124(1) of the Australian Uniform Companies Act 1961 was virtually identical the critique of *Byrne v Baker* applied generally to the law in place at that stage. It should be noted that the *Byrne v Baker* in actual fact dealt with the injustices caused by the fact that the charges against the respondent were for committing *several* offences for alleged breaches of the statutory duty contained in s 107(1). The respondent argued that only once offence could be committed if in breach of s 107(1). A major part of the case, which was probably the ratio, deals with the meaning of the part “at all times act honestly and use reasonable diligence” in s 107(1). Did that require “reasonable diligence” “at all times” or only to act “honestly” at “at all times”? It was because of these points that the court rejected the argument that there were several offences and spent quite a bit off time to show the injustices toward the defendant flowing from the fact that the charges were drafted erroneously.⁹⁷ However, the court, in trying to establish what standards were expected of a director under s 107(1), as an obiter in my view, interpreted s 107(1), in context of the *City Equitable Fire Insurance* case.

As part of its observations in passing, the court noted that the omission of “skills” in s 107(1) was significant and concluded that in actual fact “[w]hat the legislature by the subsection is demanding of honest directors is diligence only; and the degree of diligence demanded is what is reasonable in the circumstances and no more”.⁹⁸ This obviously caused considerable concern among the legislature and commentators as it was surely not intended by the legislature to lower the already low standards of care, skill and diligence expected of directors under the English-influence common law.⁹⁹

Section 124 of the Australian Uniform Companies Act 1961¹⁰⁰ was later taken up in s 229 of the Companies Act 1981 (Cth).¹⁰¹ The original provision (s 107 of the Victorian Companies Act 1958 and s 124 of the Australian Uniform Companies Act 1961) was split into two different subsections, namely s 229(1) and (2):

229. (1) An officer of a corporation shall at all times act honestly in the exercise of his powers and the discharge of the duties of his office.

Penalty-

⁹⁶ [1964] VR 443

⁹⁷ *ibid* 452 (bottom of page) et seq.

⁹⁸ *ibid* 450.

⁹⁹ See Cooney Report 25 para 3.19.

¹⁰⁰ The Uniform Companies Act 1961 was based on the Victorian legislation – see J Cassidy, *Corporations Law: Text and Essential Cases* (2nd ed, 2008) at 4.

¹⁰¹ See J Cassidy, *Corporations Law: Text and Essential Cases* (2nd ed, 2008) at 4 for an explanation how the Companies Act 1981 (Cth) applied and how it was adopted by each state. See http://www.austlii.edu.au/au/legis/cth/num_act/ca1981107/s1.html for the Companies Act 89 of 1981 (ACT), which applied in the Australian Capital Territory.

- (a) in a case to which paragraph (b) does not apply - \$5,000; or
- (b) where the offence was committed with intent to deceive or defraud the company, members or creditors of the company or creditors of any other person or for any other fraudulent purpose - \$20,000 or imprisonment for 5 years, or both.

(2) An officer of a corporation shall at all times exercise a reasonable degree of care and diligence in the exercise of his powers and the discharge of his duties.

Penalty: \$5,000.”

It will be noted that it was now made a criminal offence if the breach of s 229(1) met the requirements set out in s 229(1)(b) — “where the offence was committed with intent to deceive or defraud the company, members or creditors of the company or creditors of any other person or for any other fraudulent purpose”. Because of *Byrne v Baker*, the new statutory provision introduced an expanded objective standard by replacing the wording “reasonable diligence” with “a reasonable degree of care and diligence” in s 229(4).¹⁰² It is, interesting to note that the comments in *Byrne v Baker* regarding the omission of “skills” were apparently not taken on board by the legislature in enacting s 229(4) of the Australian Companies Act 1981. These provisions were then taken up in s 232(2)-(4) of the Corporations Act 1989:

“232(2) An officer of a relevant body corporate shall at all times act honestly in the exercise of his or her powers and the discharge of the duties of his or her office.

(3) The penalty applicable to a contravention of subsection (2) is:

- (a) if the contravention was committed with intent to deceive or defraud the company, members or creditors of the company or creditors of any other person or for any other fraudulent purpose-\$20,000 or imprisonment for 5 years, or both; or
- (b) otherwise-\$5,000.

(4) An officer of a relevant body corporate shall at all times exercise a reasonable degree of care and diligence in the exercise of his or her powers and the discharge of his or her duties.”

Again, in terms of s 299 (10), s 229 had “effect in addition to, and not in derogation of, any rule of law relating to the duty or liability of a person by reason of his office or employment in relation to a corporation and does not prevent the institution of any civil proceedings in respect of a breach of such a duty or in respect of such a liability”.

At the end of 1989 an influential Report, the Cooney Report was released.¹⁰³ This Report contained some specific recommendations on directors’ duty of care and diligence in Chapter 3. In analysing the case law and how directors’ duty of care and diligence was perceived at that stage, it was concluded that the standards expected of directors in the past, did not match the standards which the community expects of modern company directors.¹⁰⁴ The Cooney Report made a firm recommendation that “an objective duty of care for directors

¹⁰² See Cooney Report 25 para 3.19.

¹⁰³ Senate Standing Committee on Legal and Constitutional Affairs, *Company Directors’ Duties—Report on the Social and Fiduciary Duties and Obligations of Company Directors* (Cooney Report), 1989

¹⁰⁴ Cooney Report 19 para 3.2, 22 para 3.9, 28, para 3.24.

be provided in the companies legislation”.¹⁰⁵ The Report also made a definite recommendation that a “business judgment rule be introduced into Australian company law”. It was said that such a rule

“should include an obligation on directors to inform themselves of matters relevant to the administration of the company. They should be required to exercise an active discretion in the relevant matter or, alternatively, to show a reasonable degree of care in the circumstances.”¹⁰⁶

Some of the other recommendations of the Cooney Report included that “directors be required to attend board meetings unless there is a reasonable excuse to non-attendance”;¹⁰⁷ that provisions should be included in company legislation to discourage the appointment of “figurehead directors”;¹⁰⁸ and that “the companies legislation be amended to provide for, and specifically limit, the extent to which company officers may rely on others”.¹⁰⁹

In response to the Cooney Report, s 232(4) was amended in an attempt to ensure a more objective approach to directors’ duty of care and diligence. This was done in 1992 by way of s 11 of the Corporate Law Reform Act 1992, amending s 232(4) as follows:¹¹⁰

"232(4) In the exercise of his or her powers and the discharge of his or her duties, an officer of a corporation must exercise the degree of care and diligence that a reasonable person in a like position in a corporation would exercise in the corporation's circumstances."

It is significant to note that at the same time this section was decriminalised! A breach was only considered to be a breach of a civil penalty provision. The other significant change was that the words “a reasonable degree of care and diligence” was replaced with the more objective approach of “the degree of care and diligence that a reasonable person”. Also, the review of a breach of directors standard of care and diligence now were to be judged comparing the action of the director who is alleged to be in breach of his or her duty of care and diligence with a person “in a like position in a corporation” and how that person “would exercise his or her powers and the discharge his or her duties “in the corporation's circumstances”. Also here, it is clear that the intention of the legislature is to compare apples with apples. It should be remembered, as the Cooney Report so appropriately pointed out:

“There is no objective common law standard of the reasonably competent company director, as there are objective standards for other professions. It is not an easy task to determine uniform minimum standards of behaviour for company directors. The activities of companies are diverse and consequently a range of skills and experience is useful on boards, but, if the modern company director wants professional status, then professional standards of care ought to apply.”¹¹¹

and

¹⁰⁵ Cooney Report 29 para 3.28.

¹⁰⁶ Cooney Report 31 para 3.35.

¹⁰⁷ Cooney Report 32 para 3.39.

¹⁰⁸ Cooney Report 33 paras 3.41 and 3.42.

¹⁰⁹ Cooney Report 36 para 3.53.

¹¹⁰ See also Explanatory Memorandum to Corporate Law Reform Act 1992.

¹¹¹ Cooney Report 28 para 3.25.

“It may be easy to require directors of large public companies to show higher standards in their duty of care than directors of the small proprietary company, but what is required will inevitably be affected by the particular circumstances - the size, structure and sphere of operation of the company, the composition of the board and the distribution of responsibility among board members, for example.”¹¹²

The most significant change when the duty of care and diligence was taken up in the Australian Corporations Law (now the Australian Corporations Act 2001) as s 180, was the introduction of the “business judgment rule” in s 180(2). Section 180(1) dealing with the duty of care and diligence as such, was reformatted and reformulated slightly, but no substantive changes were made as would be apparent — see section 180 of the Australian Corporations Act 2001 quoted above.

(3) *Common law and statutory protection for directors as far as their duty of care and diligence is concerned*

To be completed if time and space permit!

IV SOME COMPARISONS AND SOME CONCLUSIONS

The South African and Australian law regarding directors’ duty of care, skill and diligence were both influenced considerably by English precedent of the late 1800s and early 1900s. This meant that for almost a 100 years there were very little difference how these duties were perceived in the two jurisdictions. Although Australia was far ahead of South Africa in expressing the duty of diligence in legislation (s 107 of the Victorian Companies Act 1958), the way the courts interpreted this statutory duty *Byrne v Baker* revealed that the statutory duty of diligence lowered the standards of care expected of directors even further. That was, of course, a totally unintended result. However, even in 1992, with Roger CJ’s decision in *AWA v Daniels*, it seems as if the standards of care and diligence expected of directors under the Australian common law, was still remarkably low. It is interesting to note that it was almost exactly at the same time that the Cooney Report (1989) promoted more objective standards of care for directors, and parliament introduced a more objective statutory standards duty of care and diligence (s 232(4) of the Corporations Law as amended by s 11 of the Corporate Law Reform Act 1992), that the rather conservative decision of Rogers CJ was handed down.

Also in South Africa the courts adopted a conservative approach towards directors’ duty of care, skill and diligence. *Fisheries Development Corporation*, even though decided in 1980, is still today the leading South African case on directors’ common law duty of care, skill and diligence. Also, *Fisheries Development Corporation* is still the leading South African case on directors common law duty of care, skill and diligence, even though, on a particular issue like the distinction between the duties of executive and non-executive directors it was overruled in a case like *Howard v Herrigel*.

As stated before, *Daniels v Anderson* represents the pinnacle in Australia (and probably also in other jurisdictions influenced by English law!) of the development of directors’ duty of care, skill and diligence that only started to emerge in greater detail in about 1869 with the case of *Turquand v Marshall*. *Daniels v Anderson* was decided in 1995 and since then it can safely be stated that the standards of care expected of Australian directors

¹¹² Cooney Report 28 3.27.

under the common law, raised considerably — *Daniels v Anderson* brought an abrupt end to the notion that directors’ duty of care, skill and diligence should be judged subjectively and that their negligence “must be in a business sense culpable or gross” under the common law.

Although no South African court had the opportunity in recent times to revisit the basis of liability of directors’ duty of care, skill and diligence, it has been argued above that the basis of liability is indeed delictual. If this is accepted, it is not hard to predict that if the opportunity would arise for a South African court to consider whether a director is in breach of his common law duty of care, skill and diligence, that the form of fault that will be required will be negligence as judged against the standards of a reasonable person. In determining whether such a director acted wrongfully, the court will use the well-accepted standards of the legal conviction of the community (*boni mores*). Thus, although the general English law orientated duty of care doctrine has been rejected by South African courts and South African academics, it is submitted that equally high standards of care, skill and diligence are in actual fact expected of South African directors. In this sense, the dangers for South African company directors are more concealed because of the lack of cases, but the fact that the dangers are there, cannot be denied — using an African analogy, it could be said that one should never think that there is no danger in the bush if one cannot see the leopard in the bush simply because the leopard can camouflage itself better than probably any other dangerous predator!

Australia was indeed far ahead of any English-speaking jurisdiction expressing directors’ duty of diligence in a statutory provision as early as 1958. As mentioned, however, the case of *Byrne v Baker* was a rude awakening when the original statutory provision was interpreted as having lowered the standards of diligence expected of directors. This was soon rectified by using the words “reasonable degree of care and diligence” instead of only “reasonable diligence” (s 229(2) of the Companies Act 1981 (Cth)). Since then, the Australian legislature has been determined to objectify the statutory standards of care expected of directors. This was achieved by way of amending s 232(4) of the Corporations Law in 1992 (s 11 of the Corporate Law Reform Act 1992). Section 180(1) of the Australian Corporations Act 2001 currently contains the objectified statutory duty of care and diligence.

In South Africa there has never been any attempt to express directors’ duties in general company law legislation. However, s 43 of the Close Corporations Act 69 of 1984 could be seen as a pretty good expression, in legislation, of how directors’ duty of care, skill and diligence was perceived in South Africa. Section 60 of the South African Banks Act 94 of 1990 is another example where the duties of bank directors are expressed in a statute. Currently, it is clause 76(3) of the South African Companies Bill 2008 that contains the statutory duty of care, skill and diligence.

A comparison between s 180(1) of the Australian Corporations Act 2001 and clause 76(3) reveal a few interesting things. First, the word “skill” has been retained in clause 76(3), while there has never been any “duty of skill” required of directors in terms of any predecessor of s 180(1) of the Australian Corporations Act 2001. Second, Clause 76(3) of the South African Companies Bill 2008 clearly maintained subjective elements — “having the general knowledge, skill and experience of that director”. Is this a bad thing?

As pointed out in the discussion above, the aim of the South African legislature with clause 76(3)(c) is to ensure that apples are compared with apples. I have consistently argued as part of the International Reference Group assisting the South African Department of Trade and Industry in the Corporate Law Reform since 2004, that I favour the objective approach of s 180(1) of the Australian Corporations Act 2001. There is, however, one very strong argument that made me realise that a requirement like “having the general knowledge, skill

and experience of that director” is not in actual fact a bad thing in context of the current South African situation.

Although massive progress has been made, especially through the Black Economic Empowerment (BEE), to address some inequalities that existed in the past in South Africa, it requires no in-depth research or knowledge of South Africa to realise that there is still a long way to go in South Africa. Especially as far as knowledge, skills and experience to run, manage and direct companies are concerned, a large percentage of the South African population lags far behind the majority of the population in developed countries. In other words, to measure a breach of directors’ duty of care, skill and diligence against subjective criteria, is not as silly a proposition as it would seem at first. This is specifically so because, as I have argued above, clause 76(3) succeeds in introducing a two-stage approach: The court will *first* have to determine what the expectations are of directors “carrying out the same functions in relation to the company as those carried out by that director (director whose conduct is scrutinised)” (s 76(3)(c)(i)). *Then*, the court will also have to make a value judgment as to how other directors, with “the general knowledge, skill and experience of that director (director whose conduct is scrutinised)” (s 76(3)(c)(ii)), would have conducted themselves. This approach will ensure that directors with more “general knowledge”, more “skill” and more “experience” will be judged objectively against the standards set by directors with similar “general knowledge, skills and experience”. And, in similar vain, that directors with less “general knowledge”, less “skill” and less “experience” will be judged objectively against the standards set by directors with similar “general knowledge, skill and experience”. There seems to be a lot of merit in doing so in the South African context.

Apart from many other reasons given for the “low standards” expected of directors by the English courts in the late 1800s and early 1990s, the thought of how daunting it is to manage and direct large companies, must have often crossed the minds of the English Lords. Most probably, when the Lords also realised that the knowledge, skills and experience of ordinary citizens were required to ensure that rubber companies; shipping companies; railway companies; electricity companies; companies established for the public good (“water works, gas works, roads, bridges, markets, piers, baths, wash houses, workmen’s lodge houses, reading rooms, clubs ...”) ¹¹³ etc, it must have crossed the minds Lords that if the standard of care, skill and diligence is set too high and, if these ordinary citizens could be held liable too easily, nobody (especially not ordinary citizens!) would take up positions as company directors. Similar arguments now seem to me to provide very good justification, at least for the moment, to defend clause 76(3) of the South African Companies Bill 2008 in its entirety!

¹¹³ Se JJ du Plessis “Corporate law and corporate governance lessons from the past: ebbs and flows, but far from ‘The end of History ...: Part 2’” (2009) 30 *Company Lawyer* 70 at 71-72.

A TRIBUTE TO OUR MUCH LOVED PROFESSOR, MIKE LARKIN

We write on behalf of the law students of UCT, and in particular those who were taught by the late Professor Mike Larkin. It was with great sadness, shock and anger that we woke on Saturday morning to hear news of the violent mugging and murder of our much loved law lecturer. He was a gentleman of the highest calibre, well-respected for his fine legal mind and absolute integrity. Perhaps his most enduring legacy was his modesty, humility and ability to listen.

It is on this note that we, Professor Larkin's students, appeal to the community to take a stand against violent crime in our society. For a renowned professor, returning home from an animal anti-cruelty gathering, to be heinously robbed of his own life should offend us all. Furthermore, the fact that this incident occurred merely a few hundred metres away from the local Police Station speaks volumes in itself. What hope have ordinary citizens if stalwarts of our community, upholders of not only the letter but also the spirit of the law, suffer the indignity of murder at their very doorstep?

This is the country we live in. It is a place where one is brutally murdered for the bag that they are carrying. It is a place where a man is left on the side of the road to die. It is a place where heartless, violent acts such as those which Professor Larkin endured on Friday evening are becoming increasingly common-place, and to which we, the public, are accepting with a sigh (and nothing more) as 'the reality of life'. We have chosen this reality, through our votes and our general apathy towards political and judicial issues. Violent crime is discussed too often in offices, at shopping malls, dinner parties, taxi and bus commutes and social gatherings, and yet it continues to happen, and in an increasingly brutal manner.

Professor Larkin's death is in an indicator – a symptom of an ill society, and in recognising that fact, we as a community should be prepared and willing to assist in its treatment. We can no longer continue with the attitude that our individual voice is just one of millions. Every individual in this country lives in a free democracy with constitutionally entrenched human rights, most notably those of freedom, dignity and security of person. We need to take responsibility for our sick society and make certain that those in power, entrusted with the care and enforcement of our rights, are held to account for conduct inconsistent with their maintenance.

This is our plea as students of law. It should be the legacy that we leave, and our efforts should be a tribute to the memory of a truly distinguished man, and a fine lawyer – Professor Mike Larkin. His death has profoundly affected us all; the education we received from him was so much more than the contents of the syllabus.

May you rest in peace Professor; it was an absolute privilege to have been taught by you.

UCT LAW STUDENTS: INTERMEDIATE AND FINAL YEAR CLASS 2007