



STRATLAW

Strategic Legal Advisors

Directors Manual

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1. The Companies Act 71 of 2008 and regulations and King IV™

The Governance of companies, both private and public companies is largely regulated by the Companies Act and Regulations, in cooperation various other legislation, but mainly it is regulated by the Companies Act and Regulations. Or the new act and regulations, which replaced the old act and various other legislation that dealt with the governance of companies, such as the Closed Corporation Act etc. Although some parts of the Closed Corporations Act are still in force, for all other tends and purposes, apart from the fiduciary duties of members, the Closed Corporation Act have been replaced by the new act. Because, in terms of the new act, no new close corporation can be registered. It is either a profit company or a non-profit company.

The Companies Act provides the boundaries within which a company must be governed, and the regulations provides clarity on how the companies must be governed within these boundaries. They provide more information on how to govern in a good and ethical manner as encouraged by the King IV™ report. An example is the establishment of board committees, The different sections in the act indicates when a committee must be established, but the regulations indicate how these committees are to be put together and what the purpose and objective of each committee ought to be.

Although King IV™ is not legislation, many companies have already adopted the proposals and methods put forward by the King IV™ report. In essence the main purpose of the King IV™ report is to cultivate a culture of good and ethical corporate governance of entities. Further to this, the principles and methods mentioned in the King IV™ report are held in high standard by corporate governance and compliance practitioners worldwide, it is therefore a good business decision to implement the principles and methods mentioned in the King IV™ report.

2. Director and Shareholder

A Director can be a shareholder and a director, or a director can only be a director and not shareholder and vice versa. The difference between a director and shareholder can best be described as follows: A Shareholder is one that provides capital to the entity, whereas the director is the person responsible for the day to day managing of the entity.

The director/s of a company are the key people entrusted by law with the function of administering the company and are central to ensuring good and ethical corporate governance of the company.

The Act extends the definition of “director” to include others, which has a particular impact regarding duties, potential liability and responsibility of directors and officers.

The definition is extended to include prescribed officer, a person who is a member of a committee of a board of a company, or the audit committee of a company (irrespective of whether the person is also a member of the company's board).

For purposes of Section 69 (qualification and eligibility), section 76 (standards of directors' conduct), Section 77 (directors' liability), section 78 (indemnification and directors' insurance) the definition of "director" is extended to include alternate director, prescribed officer, a person who is a member of a committee of a board of a company, or is a member of the audit committee of a company (irrespective of whether or not the person is also a member of the company's board).

With reference to indemnification and directors' insurance, the definition also includes former director(s). Section 75 also extends the definition of director to certain person, as more clearly defined.

Those designated officers as described above are subject to the same standards of conduct, duties of care, skill and diligence and fiduciary duties as directors, and will be held jointly and severally liable with directors. The MOI and any additional rules are also specifically binding between the company and such officers.

The rights and duties of both the shareholder and director differs in many instances, however for purposes of this manual only the duties and responsibilities of a director will be discussed and explained with practical examples.

3. Duties of Director/s

There are various duties a director has in terms of the Companies Act and Regulations and various other legislation such as the Protection of Personal Information Act, however the most important part of the duties of a director is the fiduciary duties imposed by Section 76 of the Companies Act. These are also known as the common law duties as they were previously referred to before the new companies act.

Fiduciary Duties:

- To act bona fide in the interests of the company
- To exercise powers for their proper purpose
- To exercise independent judgement in decision making
- Not use corporate property information or opportunities for personal profit
- Duty to disclose any conflict of interest

- ❖ Duty to position and use information for company's benefit, and not for his own private advantage or the advantage of any other person other than the company or a wholly owned subsidiary of the company.
- ❖ Duty to disclose material information [unless he reasonably believes the information is immaterial to the company or generally available to the public or known to other directors or is bound not to disclose the information by legal or ethical obligation of confidentiality].
- ❖ Duty to perform duties in good faith, in the best interests of the company and with due care, skill and diligence that would reasonably be expected of a person carrying out the same functions in relation to the company as those carried out by that director and having the general knowledge skill and experience of that director.

The consequences of contravening the fiduciary duties will result in the director being declared delinquent or subjected to a probation order subject to certain conditions. A delinquency order may be for lifetime, if circumstances permit, but usually a delinquency order is for seven years or longer. Upon the issuing of a delinquency order or probation order the court has the power to attach certain conditions to said order.

The overflowing consequences of a delinquency order or probation order is that for the period for which the order is in effect, the person in respect of which the order has been issued, will be disqualified to be a director of a company, and may not act or be appointed as a director of a company.

Further to the above, the risk of appointing a previously declared delinquent director or a person who was placed on probation, will in many cases be too big for company to take on and will most probably steer clear of appointing such person as a director.

If a company appoints a person whilst said person has been declared a delinquent director and the period mentioned in the court is still in effect, the other directors who appointed the director will also be placed in a situation to be declared delinquent directors and may be held personally liable for any damages that the company may or might have suffered due to this appointment.

4. Fiduciary duties

The fiduciary duties of directors were always part of the common law and was never stipulated in law. This changed with the implementation of the new Companies Act. The new Companies Act took various common law principles and incorporated them into legislation called the Companies Act and Regulations.

The fiduciary duties are those duties that one normally would expect to be part of any person let alone of a director of a company.

- **To act bona fide in the interests of the company**

To act bona fide in the interests of the company, means to always act in the best interests of the company. A practical example of this is when a director is part of a conversation where the company, he is a director off is the subject of conversation, and the director either talks negatively of the company or discloses negative behaviour towards the company to such an extent that those taking part in the conversation questions the director's loyalty to the company.

- **To exercise powers for their proper purpose**

With this duty a director is required to use the authority he has for the purpose it has been given to him. By appointing a person without following the necessary process and procedures, just because the director knows the person and without there being a valid reason, is an example of not exercising his powers for its proper purpose.

- **To exercise independent judgement in decision making**

A director must always when it relates to company matters exercise independent judgment. This entails that when a director is required to decide the decision must be made based on the merits of the issue and act according to their discretion in the best interests of the company. Therefore, when a director is required to purchase a new company vehicle or not, the decision to purchase or not should be based on the financial position of the company whether the company can afford it or not. If the company can afford it, and it will add value to the company for having the new company vehicle, that can be seen as a valid reason for the purchasing of the vehicle. However, if the company cannot afford it and it will not add value to the company then it will not be seen as a valid explanation as to why the company need the company vehicle.

- **Not use corporate property information or opportunities for personal profit**

As a director of a company, the director will become privy of certain information or opportunities. It is the duty then of the director to use the information or the opportunity to the benefit of the company and not for personal benefit or profit.

For example, if the company of the director is a second hand car dealership, and the director knows of a person that is willing to buy the vehicle, but said person does not want to buy it from a car dealership but from a private person, then the director cannot sell the vehicle to the third party on a private basis and take the profit of the sale for his/her personal profit. The director has a duty to sell the vehicle through the company and let the company receive the benefit of the transaction.

- **Duty to disclose any conflict of interest**

Whenever a conflict of interest appears, it must be disclosed by the director unless it has no bearing on the company of which the director is a director.

A conflict of interest can take on many forms. The various conflicts of interests will be discussed in detail further below. But, for purposes of this section a conflict of interest can be explained as where a family member appoints another family who is unqualified to perform the duties said family member has been appointed or when a company of which you are a director submits a tender to provide services to the other company you are a director of.

5. Conflict of Interest

As mentioned, a conflict of interest can take on many forms especially when it comes to the governance of a company. But, in a governance sense, a conflict of interest means any financial or other interest that not only actually but also potentially impairs a director's objectivity and his ability to act independently, or creates an unfair advantage for, or in favour of said director. Conflict of interest usually only applies to current interest and not interest that have passed or no longer exists, or if it is a current interest, an interest that will not affect the director's current behaviour unreasonably. It is imperative to note, that a conflict of interest is not illegal or unlawful, it how it is dealt with or what is or has been done when a conflict of interest is or has presented itself, that is illegal or unlawful. The failure to disclose or deal with a conflict of interest is the illegal or unlawful act.

There are numerous examples of conflict of interests. The most common conflicts of interests are discussed below.

Nepotism

This is when a family member or a close friend of a director is appointed, promoted, or otherwise receives special treatment due to the personal relationship with the Director. Nepotism is seen as a conflict of interest because the family member or close friend receives preferential treatment which said person would not normally receive if it was not for the relationship with the director.

Self – dealing

Self – dealing is when a director who has financial information regarding the company uses the knowledge or information to benefit the director personally over the objectives of the company.

Financial

A financial conflict of interest is where a director of a company holds shares in a company which contracts with the company of which the person is a director of.

The above conflicts are the most common conflicts that is experienced on a daily basis within a company. In terms of Section of the Companies Act, it is a director's fiduciary duty to disclose a conflict of interest. Failure to disclose a conflict of interest, regardless of the conflict-of-interest results in non – compliance with the relevant

section of the act, therefore the failure to disclose results in the director not complying with his/her fiduciary duties. This is grounds for the director to be declared a delinquent director.

If a director is not sure whether to disclose the conflict or not, it is advisable to err on the side of caution and rather disclose the conflict and let the board make a decision than not disclosing and the conflict.