

# The Legal Nature of the Duty of Care and Skill: Contract or Delict?



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## Abstract

This article evaluates the legal nature of the duty of care and skill of directors. In terms of the *Companies Act* 71 of 2008 this duty is essentially delictual in nature. This article evaluates whether the duty is in fact delictual in nature. Case law, which considered the duty of care and skill and where it had been sought to establish liability for directors, has in fact mainly been in respect of non-executive directors. A clearer distinction should therefore be drawn between executive and non-executive directors whose duties would be more of a contractual nature. The article then evaluates whether the legal nature of the duty of care and skill would lead to any practical difference depending on the cause of action.

## Keywords

Duty of care and skill; executive directors; non-executive directors; contract; delict; concurrence of claims

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## 1 Introduction

Section 77(2)(b) of the *Companies Act*<sup>1</sup> (the Act) provides that a director of a company may be held liable based on the common law principles relating to delict for any losses or damages which the company may suffer due to a breach of the duty of care and skill in terms of section 76(3)(c), losses due to a breach of a provision of the Act not mentioned in section 77 and losses due to the contravention of any provisions of the memorandum of incorporation (Mol) of the company. This article poses the question whether the legislature was correct in formulating the legal nature of the duty of care and skill as well as the liability of directors for losses flowing from any breach of the company's Mol as delictual. The article will attempt to show that the basis for liability is not necessarily delictual in nature, but that it could be argued that the basis could also be contractual.

To be able to determine what form of liability, ie contractual and/or delictual, there should be for directors, it is important to first determine what is meant by the term "director". In this respect the article will not deal with issues like *de facto* directors but with the concepts of executive and non-executive directors. Whether the fact that a director's status is that of a *de facto* director would produce a different outcome is debatable. A *de facto* director is still a director, even if he has not been formally appointed as such. The fiduciary duties, duty of care and skill and Mol would still be binding on him.<sup>2</sup> It is therefore arguable that there is still some form of contractual arrangement with him, to note the Mol. The question is whether there are different standards of liability depending on the type of director who is acting. Whether there is indeed a difference in the basis of liability then gives rise to the question of whether it is correct that there are different standards of liability for executive and non-executive directors.

## 2 Executive and non-executive directors

The Act only refers to a director, which term is defined as

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<sup>1</sup> 71 of 2008.

<sup>2</sup> See generally Blackman, Jooste and Everingham *Commentary on the Companies Act* RS 9, 2012 at 8-4 and RS 6, 2009 at 8-5.

... a member of the board of a company, as contemplated in section 66, or an alternate director of a company and includes any person occupying the position of a director or alternate director, by whatever name designated.<sup>3</sup>

No formal distinction is made between executive and non-executive directors. The Act refers to and defines an *ex officio* director as

... a person who holds office as a director of a particular company solely as a consequence of that person holding some other office, title, designation or similar status specified in the company's Memorandum of Incorporation.<sup>4</sup>

The terms "executive" and "non-executive" directors are well established. The origin of the distinction is not clear, however. The King Code of Governance for South Africa 2009 (King III) differentiates between executive and non-executive directors. It provides that the board is responsible for corporate governance and has two main responsibilities, namely to determine the strategic direction of the company and to exercise control over the company. Importantly it states that the board requires management to execute strategic decisions effectively.<sup>5</sup> King III further states that the board is responsible for the fact that management ensures that a culture of ethical conduct is present and that it should set values to which the company will adhere.<sup>6</sup> From these two points it would appear that King III is referring to non-executive directors when it refers to the "board", or at least part of the board as a whole, and that the term "management" refers to the executive directors.<sup>7</sup>

However, in point 14 of Chapter 1, King III refers to the "board" and the "executive management". Principles 2.1 and 2.2 differentiate between the terms "board" and "management". Principle 2.18 differentiates between executive and non-executive directors. Crucially the board consists of these two types of directors. The focus of principle 2.18 appears to be on non-executive directors and their role on the board of a company. Interestingly enough, hardly any mention is made of the make-up of management. In principle 4.4 it is stated that the board should delegate the design, implementation and monitoring of the risk management plan of the company to management.<sup>8</sup> When one looks at King III as a whole there is always a clear distinction that is made between the "board" and "management". Only in a few principles are the terms "executive" and

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<sup>3</sup> Section 1 of the Act.

<sup>4</sup> Section 1 of the Act.

<sup>5</sup> Chapters 1, 7 of IoDSA *King Report* (King III).

<sup>6</sup> Chapters 1, 8 of King III.

<sup>7</sup> See also point 10 of Chapter 1 of King III.

<sup>8</sup> Also see principle 4.7 in respect of risk responses and principle 4.8 in respect of continual risk monitoring by management.

"non-executive" used. From the context of the use of the term "management," the term would appear to mean the executive directors, whereas the board as a whole is referred to under the term "board".

As mentioned before, the Act also does not distinguish between executive directors and non-executive directors. It refers only to "directors". The *Companies Act*<sup>9</sup> (the 1973 Act) also did not make this distinction. However, there is one crucial difference with the Act in this respect. Table A and Table B of the 1973 Act provide:

The directors may from time to time appoint *one or more of their body* to the office of managing director or manager for such term and at such remuneration (whether by way of salary or commission or participation in profits or partly in one way and partly in another) as they may think fit and may revoke such appointment subject to the terms of any agreement entered into in any particular case. A director so appointed shall not, while holding such office, be subject to retirement by rotation, or taken into account in determining the rotation of retirement of directors; but his appointment shall determine if he ceases for any reason to be a director.<sup>10</sup>

It is arguable that the emphasised portion of the above quotation indicates that the board as a whole may appoint directors to manage the company; ie, to appoint executive directors from their rank. The quotation should therefore not be interpreted to mean only a managing director like a Chief Executive Officer, but a director or directors who manage. This is what happened in practice. Directors/employees of the company were and are appointed by the board. The Act does not provide for this power of the board, however. The closest the Act comes to this is in the wording of section 66(1). This provision states that:

The business and affairs of a company must be *managed by or under the direction of its board*, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that this Act or the company's Memorandum of Incorporation provides otherwise.<sup>11</sup>

The emphasised part of section 66(1) may provide wide enough power for the board to delegate the day-to-day management to the executive directors, but the board as a whole has a supervisory role.

*Fisheries Development Corporation of South Africa Ltd v Jorgensen*<sup>12</sup> is the *locus classicus* in South African law dealing with the duty of care and

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<sup>9</sup> 61 of 1973.

<sup>10</sup> Table A 61 and Table B 62 of the *Companies Act* 61 of 1973 (the 1973 Act). Emphasis added.

<sup>11</sup> Emphasis added.

<sup>12</sup> *Fisheries Development Corporation of South Africa Ltd v Jorgensen* 1980 4 SA 156 (W) (*Fisheries Development Corporation*).

skill of directors of a company. Amongst other matters, the court set out the differences between executive and non-executive directors. It stated that the duties of non-executive directors are those that are of an intermittent nature which are performed at board meetings. The non-executive director is not involved in the day-to-day management of the company and he does not have to have any special business acumen or even business knowledge of the specific business of which he is a director.<sup>13</sup> He may further delegate and rely on the judgement of others in management. However, he still has to exercise his own judgement on a matter and cannot blindly follow advice.<sup>14</sup> Executive directors, on the other hand, are involved in the day-to-day running of the business of the company. Crucially, the court does not state whether the determination of whether the duty of care and skill has been breached differs depending on the type of director. In a sense it states that the determination is different by saying that the duty of care and skill (or its breach) depends upon whether the director is executive or non-executive, but it does not then state how to apply any different possible tests.<sup>15</sup>

Where does this distinction come from? As early as in 1884, and probably even earlier, the distinction between an executive and a non-executive director was known. In *Re Denham & Co*<sup>16</sup> the articles of the company conferred great powers on Denham, whereas the other director, Crook, was not involved in the day-to-day management of the company. In today's parlance Crook was a non-executive director. Denham committed fraud on the company and an attempt was made to hold Crook liable. The court held, however, that Crook could not be held liable because he had not attended a single meeting during the course of the four years when the fraud was perpetrated on the company. The court held that:

Mr Crook, who was a country gentleman, and not a skilled accountant, discovered nothing. These rogues, in short – for roguery it was – put before him so much that he came away with as little information as he possessed when he went. I am satisfied that if Mr Crook had endeavoured during the period in question to make an investigation, the investigation would have ended in the same way.<sup>17</sup>

In *Re Cardiff Savings Bank (Marquis of Bute's Case)*<sup>18</sup> the Marquis was the president of the bank. The articles provided that the business of the

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<sup>13</sup> *Fisheries Development Corporation* 165H-166B.

<sup>14</sup> *Fisheries Development Corporation* 166E.

<sup>15</sup> *Fisheries Development Corporation* 165H-166B.

<sup>16</sup> *Re Denham & Co* 1884 25 Ch 752 (decided on 20, 21 and 26 November 1883).

<sup>17</sup> *Re Denham & Co* 1884 25 Ch 752 777-778.

<sup>18</sup> *Re Cardiff Savings Bank* 1892 2 Ch 100 (*Marquis of Bute's Case*).

bank would be conducted by the president, trustees and managers. The Marquis never participated in any meetings. The court, however, stated that:

... the standard of duty for an unpaid trustee or manager of a savings bank ... cannot, I think, be placed higher than that of a director of a trading company, who usually receives remuneration and is a member of a much smaller body.<sup>19</sup>

The court then further stated "I think that the Marquis was entitled to rely on the trustees and managers who took part in these meetings".<sup>20</sup> Despite the fact that according to the articles the Marquis was part of management, he *de facto* became a non-executive director and therefore no liability accrued due to the fact that he never attended meetings where accounts were presented and discussed. He could therefore never have discovered any fraud.

The *In Re Brazilian Rubber Plantations and Estates, Limited*<sup>21</sup> case was the first real attempt by an English Court to distil any sort of principle in respect of the duties of directors. The court stated that:

A director's duty has been laid down as requiring him to act with such care as is reasonably to be expected from him, having regard to his knowledge and experience. He is, I think, not bound to bring any special qualifications to his office. He may undertake the management of a rubber company in complete ignorance of everything connected with rubber, without incurring responsibility for the mistakes which may result from such ignorance; while if he is acquainted with the rubber business he must give the company the advantage of his knowledge when transacting the company's business. He is not, I think, bound to take any definite part in the conduct of the company's business, *but so far as he does undertake it* he must use reasonable care in its despatch.<sup>22</sup>

And further:

Such reasonable care must, I think, be measured by the care an ordinary man might be expected to take in the same circumstances on his own behalf. He is clearly, I think, not responsible for damages occasioned by errors of judgment.<sup>23</sup>

It would appear from this judgment that the court advocated an objective test to determine negligence on the part of the directors. But, crucially, the

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<sup>19</sup> *Marquis of Bute's Case* 109.

<sup>20</sup> *Marquis of Bute's Case* 110

<sup>21</sup> *In Re Brazilian Rubber Plantations and Estates, Limited* 1911 1 Ch 425 (*Brazilian Rubber*).

<sup>22</sup> *Brazilian Rubber* 437. Emphasis added.

<sup>23</sup> *Brazilian Rubber* 437.

court distinguished those people who took part in the conduct of the company's business from those who did not.

The *locus classicus* in respect of the duty of care and skill in English Law is *In Re City Equitable Fire Insurance Company Limited (Re City Fire)*.<sup>24</sup> The liquidators of the insolvent company attempted to hold the directors liable in terms of the misfeasance provisions of the 1908 *Companies Consolidation Act*, which essentially required wilful neglect. The articles of the company, however, also provided that no liability would accrue for directors in the discharge of their duties unless they were grossly negligent. The court then listed the now-oft quoted elements of the duties of the directors of the company.

According to the court the position of a director of a company carrying on a small business differs from that of a director of a large enterprise. In one company, for instance, matters may normally be attended to by the manager or other members of the staff that in another company are attended to by the directors themselves. The larger the business carried on by the company the more numerous and the more important the matters that must of necessity be left to the managers, the accountants and the rest of the staff. The manner in which the work of the company is to be distributed between the board of directors and the staff is in truth a business matter to be decided on business lines according to the court.<sup>25</sup>

The gist of the judgment and hence the duties of directors can be summarised as follows:

- a) A director has to exercise his duties only with the care and skill which can be reasonably expected of someone with his knowledge and experience. Errors of judgment are therefore allowed.<sup>26</sup> An inexperienced director may probably make more mistakes, even if qualified.
- b) The exercise of the duties is of an intermittent nature and essentially has to be exercised at board meetings only.<sup>27</sup>
- c) A director may delegate his duties and can trust the person to whom he has delegated the duties in the absence of suspicion.<sup>28</sup>

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<sup>24</sup> *In Re City Equitable Fire Insurance Company Limited* 1925 Ch 407 (*Re City Fire*).

<sup>25</sup> *Re City Fire* 408.

<sup>26</sup> *Re City Fire* 428-429.

<sup>27</sup> *Re City Fire* 429. This leg could probably apply only to a non-executive director according to Keay. See Keay *Directors' Duties* 207.

From the facts of the case it again appears that the directors who were sought to be held liable were the non-executive directors of the company and not the executives. This is especially the case when one considers the second point that the court made in respect of the intermittent nature of the directors' duties. This can only be in respect of part-time non-executive directors. What the early case law in England has therefore shown is that the courts recognised the distinctive roles of the executive and the non-executive directors of companies. Peculiarly the emphasis was always on the role of the non-executive directors. The role of the executive management is hardly addressed. This could be due to the fact that in all the cases mentioned it was the non-executive directors who were sought to be held liable.

The 1926 *Companies Act* provided essentially for the liability of directors where there had been a breach of duty and that the articles could not exempt the directors from liability.<sup>29</sup> According to Henochsberg, liability could therefore not be excluded in the articles.<sup>30</sup> Henochsberg refers to the liability of directors twice more in the second edition. In both instances, however, the authors refer to liability as laid down for negligence by the *Re City Fire* case, in the context of directors breaching their statutory duties in respect of the allotment of shares and the failure of the company to keep (proper) books and accounts. The author does not use the case as authority for any harm that the company suffers in delict but purely where the director has not complied with a statutory provision. The question was therefore whether the director was negligent in breaching a statutory obligation.

In the first edition of "Maatskappyereg"<sup>31</sup> the authors do not discuss the duty of care and skill in any detail but only refer to the *Re City Fire* case. They do mention, however, that not all the comments made in the *Re City Fire* case apply to all directors. The statement of the court that the duties of a director are of an intermittent nature does not apply to directors who are employees of the company or to a director who in terms of his contract with the company has to give his full attention to the business of the

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<sup>28</sup> *Re City Fire* 429.

<sup>29</sup> See s 70 *sexo* of the *Companies Act*, 1926.

<sup>30</sup> Henochsberg and Fairbairn *Henochoberg on the Companies Act*. On page 177 reference is made to articles prior to 1939 which exempted directors from liability for negligence. The learned author in this instance refers to the *Brazilian Rubber* and *Re City Fire* cases.

<sup>31</sup> Cilliers and Benade *Maatskappyereg*.



company.<sup>32</sup> Under the heading "werknemers" the authors then also refer to the dual status of directors, namely as officers of the company as well as employees. The authors then state that the obligations of such directors will be determined by their positions as directors as well as their contracts of employment.<sup>33</sup> In the second edition of "Company Law"<sup>34</sup> the authors, with reference to the doctoral dissertation of Naude, state that the liability of directors is delictual in nature but that executive directors may be guilty of breach of contract as well.<sup>35</sup> The authors repeat this statement in the third edition of their book as well.<sup>36</sup> This is important, because it shows that scholarly works too indicate that there are important differences between executive and non-executive directors.

There are two theories which seek to describe the effectiveness of having a majority of non-executive directors. The managerial hegemony theory provides that management will always control the board and that the non-executives, even if independent and a majority, will be powerless to prevent management excesses.<sup>37</sup> The other theory is the effective management theory which stems from the field of financial economics and which holds that outside non-executive directors are effective in that they are desirous to protect the interests of the shareholders of the company, not necessarily in the interest of the company but of their own reputational standing. They will therefore be seen as "experts in decision control".<sup>38</sup> As mentioned above, apart from the *Fisheries Development* case there appears to be a dearth of cases in South African law dealing with the duty of care and skill and then specifically the roles of executive and non-executive directors. When one considers foreign law, in *Dorchester Finance Co Ltd v Stebbings*<sup>39</sup> the Chancery Division confirmed the dictum of Romer J in *Re City Fire* when the court concluded the following:

- a) A director is required to exhibit in performance of his duties such a degree of skill as may reasonably be expected from a person with his knowledge and experience.
- b) A director is required to take in the performance of his

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<sup>32</sup> Cilliers and Benade *Maatskappyereg* 208. Seemingly the authors refer to the executive directors.

<sup>33</sup> Cilliers and Benade *Maatskappyereg* 216.

<sup>34</sup> Cilliers and Benade *Company Law* 2<sup>nd</sup> ed.

<sup>35</sup> Cilliers and Benade *Company Law* 2<sup>nd</sup> ed 242.

<sup>36</sup> Cilliers, Benade and De Villiers *Maatskappyereg* 3<sup>rd</sup> ed 257. See also Cilliers, Benade and De Villiers *Maatskappyereg* 4<sup>th</sup> ed 335, as well as Cilliers *et al* *Corporate Law* 335 where the statement that the claim could also be contractual in the case of executive directors is repeated.

<sup>37</sup> In this regard see Lin 1996 *Nw UL Rev* 898 generally for a discussion of the effectiveness of outside independent non-executive directors.

<sup>38</sup> Lin 1996 *Nw UL Rev* 898.

<sup>39</sup> *Dorchester Finance Co Ltd v Stebbings* 1989 BCLC 498 (Chancery Division).

duties such care as an ordinary man might be expected to take on his own behalf. c) A director must exercise any power vested in him as such honestly, in good faith and in the interests of the company.<sup>40</sup>

The case involved fraud by Stebbings. Two other directors of Dorchester, Hamilton and Parsons, were non-executive directors and signed blank cheques which enabled Stebbings to do harm to the company through the misapplication of company assets. Two of the three directors were chartered accountants and Hamilton had extensive accounting experience. The court held that the non-executive directors, with their extensive accounting experience and qualifications, were negligent even if no meetings were held by the board. They could therefore not excuse themselves by pleading that they did not attend board meetings, which in fact were hardly ever held. Crucially, the court stated that the duties of directors, whether executive or non-executive, are the same in terms of the 1948 *Companies Act*.<sup>41</sup>

In *Equitable Life Assurance Society v Bowley*<sup>42</sup> the court confirmed that the duty of a non-executive director in expression does not differ from the duties of executive directors, but that the duties might differ in their application. An important point which was raised was the right of directors to delegate. The harmed company argued that although delegation may take place, the director must ultimately still supervise the delegate. On the other hand the defendants relied on *Re City Fire* where the court held that once a director has delegated, he may rely on that person. The court held that this pronouncement of the *Re City Fire* case is not in conformity with modern law. The court stated that:

It is well known that the role of non-executive directors in corporate governance has been the subject of some debate in recent years. For present purposes, as Mr Milligan submitted, it in any event suffices to say that the extent to which a non-executive director may reasonably rely on the executive directors and other professionals to perform their duties is one in which the law can fairly be said to be developing and is plainly "fact sensitive". It is plainly arguable, I think, that a company may reasonably at least look to non-executive directors for independence of judgment and supervision of the executive management.<sup>43</sup>

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<sup>40</sup> *Dorchester Finance Co Ltd v Stebbings* 1989 BCLC 498 (Chancery Division) 502.

<sup>41</sup> *Dorchester Finance Co Ltd v Stebbings* 1989 BCLC 498 (Chancery Division) 503.

<sup>42</sup> *Equitable Life Assurance Society v Bowley* 2004 1 BCLC 180; 2003 EWHC 2263 (Comm).

<sup>43</sup> *Equitable Life Assurance Society v Bowley* 2004 1 BCLC 180; 2003 EWHC 2263 (Comm) para 41. Also see *Barlows Manufacturing Co Ltd v RN Barrie (Pty) Ltd* 1990 4 SA 608 (C), where the court also held that the power to delegate does not mean that the delegator may abdicate his responsibilities over the delegate.

The Financial Reporting Council (FRC) issued its "Guidance on Board Effectiveness" in 2011. In this guidance the roles of the executive and non-executive directors are distinguished. The FRC, according to its website, sponsors the UK Corporate Governance Code and sets the standards framework within which auditors, accountants and actuaries operate within the UK and Ireland. The FRC then monitors the implementation of these standards and tries to promote best practice by companies and professionals.<sup>44</sup> The FRC requires an active monitoring role by non-executive directors and they cannot be mere passengers or spectators. They are expected to be well acquainted with the business of the company and the issues relevant to the business of the company to foster respect from the other executive board members.<sup>45</sup> The non-executive directors are furthermore expected to make enough time available to discharge their duties in an effective manner. This undertaking should ideally be included in their letters of appointment to the board, and the minimum time which is expected to be spent on the company's business should be spelt out, including further time during specific activities like fundamental transactions.<sup>46</sup> The active role that non-executive directors should play within the company includes requesting and insisting on receiving sufficient detailed information, within enough time before board meetings. This naturally is so that they can come to board meetings fully prepared to enable proper and informed debate about issues. This in turn should lead to better decision-making. The role of what is expected of a director in a specific case should also be set out in the report containing the information for the director.<sup>47</sup> What is clear from these guidelines, which accord with what the King III Report expects of non-executive directors, is that they should be pro-active monitors of the executive directors. They should actively seek and demand information prior to board meetings, which information should be detailed and should be delivered timeously to them. One would assume that this would include the active monitoring and demanding of feedback on issues/guidelines/policies which were delegated to the executive directors for implementation. The non-executive directors should demand that they be continuously informed on the implementation of these policies/guidelines on a regular basis, at the very least at board meetings, which should ideally be frequent. The

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<sup>44</sup> FRC date unknown <https://www.frc.org.uk/Our-Work/our-key-activities.aspz>.

<sup>45</sup> Guideline 1.19 of FRC date unknown <https://www.frc.org.uk/Our-Work/our-key-activities.aspz>.

<sup>46</sup> Guideline 1.20 of FRC date unknown <https://www.frc.org.uk/Our-Work/our-key-activities.aspz>.

<sup>47</sup> Guideline 1.22 of FRC date unknown <https://www.frc.org.uk/Our-Work/our-key-activities.aspz>.

frequency should probably depend on the size and complexity of the company and its business. A board of a listed company should probably meet at least once a month, whereas a board of a small non-profit company (NPC) could conceivably meet less frequently. Equally, though, the board of a NPC with a large public impact should meet more regularly than the board of a small public unlisted company whose business is confined to one place and which has few shareholders.

It is still necessary to ask, however, about the relevance of this distinction between executive and non-executive directors in respect of the duty of care and skill. In the light of the different roles that executive and non-executive directors play within a company, could it be argued that any possible breach should be determined differently depending on the type of director? What exactly does the court mean in the *Bowley* case above when it says that the duties of the respective directors do not differ in their expression but may well differ in their application? In *Daniels v Anderson*<sup>48</sup> the court stated that non-executive directors, in the discharge of their duties, must "take reasonable steps to place themselves in a position to guide and monitor the management of the company".<sup>49</sup>

Keay argues that although there is no difference between executive and non-executive directors with respect to their duties, the UK *Companies Act* does allow for a differentiation to be made between them, since the UK *Companies Act* refers to "carrying out the functions carried out by a director".<sup>50</sup> The argument is that executive directors carry out functions which are different from those of non-executive directors.<sup>51</sup> Keay pleads for a clarification of the functions of non-executives in law, because he argues that this hinders the determination of whether or not a director has breached his duties in terms of section 174 of the UK *Companies Act*. The UK Institute of Directors argued that non-executive directors face numerous challenges in their positions. These include the nature of the joint and several liability of directors, a lack of information, a lack of knowledge of the specific business and, as Keay puts it, "they don't know what they don't know".<sup>52</sup>

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<sup>48</sup> *Daniels v Anderson* 1995 16 ACSR 607.

<sup>49</sup> *Daniels v Anderson* 1995 16 ACSR 607 664.

<sup>50</sup> Keay *Directors' Duties* 257 with reference to s 174 of the *Companies Act*, 2006.

<sup>51</sup> See King III in respect of the establishment of policies by the board, including the non-executive directors, but that implementation is left to the executive directors and the rest of management.

<sup>52</sup> IoD 2004 <http://www.iod.com/influencing/policy-papers/corporate-governance/director-and-auditor-liability-7-8>; also see Keay *Directors' Duties* 258.

With all of the above in mind, the next question is how a breach of the duty of care and skill in terms of the Act should be determined. Firstly, should there be a difference in how breach is determined in common law and in terms of the Act, and secondly should there be a difference in the determination of breach of duty between executive directors and non-executive directors.

### 3 The position of executive directors

Upon a reading of King III it would appear that the focus is on the position of the board, but then specifically on the role of non-executive directors on the board. The executive directors should be a minority on the board, and they are responsible, as part of management, for implementing the policies and strategies which the board has set.<sup>53</sup> Essentially the role of executive directors is management.<sup>54</sup> Cassim *et al* also note that executive directors are full time employees of the company and are therefore involved in the day-to-day running of the company.<sup>55</sup> They will therefore have contracts of employment with the company. As King III provides, the executive together with management is there to implement strategies. This would require some form of discretion in respect of the conduct of the business, the precise practical implementation of the strategies which the board has approved of, and other practical implementation issues. Ezzamel and Watson call this the non-programmable aspects of the employment of executives.<sup>56</sup> Keay also refers to executive directors only as employees of the company who have management powers.<sup>57</sup>

With reference to *Cohen v Segal*<sup>58</sup> Cassim states that the legal nature of directors can at best be called *sui generis* and that directors are not necessarily agents, trustees or managing partners. Executive directors could simultaneously fall into any one of those categories as well as still being employees of the company. Furthermore, the employment contract of the director will not necessarily set out the rights and obligations of directors. These are also determined by the Mol of the company, the *Companies Act*, various pieces of labour legislation and the common law. The Act now specifically states that a Mol is binding on a company and its directors.<sup>59</sup> It would therefore be an implied term of the employment

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<sup>53</sup> See principle 2.18 of King III, for example.

<sup>54</sup> King III Annex 2.2.

<sup>55</sup> Cassim *et al Contemporary Company Law* 411, 477.

<sup>56</sup> Ezzamel and Watson "Wearing Two Hats" 57.

<sup>57</sup> Keay *Directors' Duties* 10.

<sup>58</sup> *Cohen v Segal* 1970 3 SA 702 (W).

<sup>59</sup> Section 15(6)(c) of the Act.

relationship that the directors act with the necessary care and skill in exercising their duties.

But what, then, does section 77(2)(b) mean when it provides that a director of a company may be held liable based on the common law principles relating to delict for any losses or damages which the company may suffer due to a breach of the duty of care and skill in terms of section 76(3)(c), losses due to a breach of a provision of the Act not mentioned in section 77, and losses due to the contravention of any provisions of the Mol of the company. Does this mean that the company has only a delictual claim, or does the company have an election between a delictual and a contractual claim? If one understands the article to imply that any claim can be only delictual, could it relate to the statutory duty of care and skill only? Would it be prudent to have a two-remedy provision? What would the point be? Let us assume that the common-law position could also be contractual. The reasons would be the following:

Does the provision mean that the law of delict applies only in respect of the remedies available for the company in cases of breach by a director, or does it mean that the law of delict applies also in respect of the determination of whether or not there has been breach – in other words, that the five elements of a delict would have to be present before a breach was present?

A short comparative study with German law will be undertaken next. The purpose of the comparative study is to show that the duty of care and skill also exists in a civil law system that has also been codified (but where the legislature did not provide for the legal nature of any claim where the duty of care has been breached). The result of this is that directors can be held liable under contract as well. Another reason for the comparison is that Germany has a two-tier board system for the *Aktiengesetz* (AG) where the company has a management board and a supervisory board (the *Aufsichtsrat*). According to Peltzer<sup>60</sup> the supervisory board is becoming more common in other company forms like the GmbH.

#### **4 The duty of care and skill in German Law**

Section 102 of the AG provides that the supervisory board is an independent body which is elected by the shareholders for a maximum period of four years. The supervisory board appoints and supervises the

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<sup>60</sup> Wellhöfer, Peltzer and Müller *Die Haftung von Vorstand Aufsichtsrat Wirtschaftsprüfer* 542.

board of directors. Supervision includes the lawfulness and commercial prudence of the activities of the management board.<sup>61</sup> The management board must report to the supervisory board at least four times per year.<sup>62</sup> Section 111 of the AG provides for the rights and obligations of the supervisory board. The supervisory board or the company's constitution may provide that certain transactions require the consent of the supervisory board.<sup>63</sup> The AG also sets out other more specific duties for the supervisory board.<sup>64</sup> The duties of the supervisory board members may also not be delegated.<sup>65</sup> The AG specifically provides that the duty of care in terms of section 93, with the exception of one sentence, applies to the members of the subsidiary board.<sup>66</sup>

Both the AG and the GmbH legislation impose a duty of care and skill on directors.<sup>67</sup> This duty encompasses what we would understand as fiduciary duties as well. The duty of care and skill is neither contractual nor delictual, but the liability is based upon the fact that a director serves as an organ of the company. The reason why it is not delictual is that pure economic loss is not possible under the German law of delict. The liability also exists outside any contractual appointment.<sup>68</sup> It exists parallel to any liability in terms of section 826 of the *German Civil Code* (the BGB), which deals with delictual liability. According to Alexander the test for liability in the GmbH legislation is objective in nature.<sup>69</sup> The liability is not joint and several but applies only to those directors who were guilty of breaching their duty.<sup>70</sup> According to Ihrig and Schaefer it does not necessarily suffice to vote against or even abstain against a measure to escape liability. If the decision is illegal or breaches the company's constitution, there may be liability.<sup>71</sup>

The German AG has also incorporated an adapted version of the Business Judgement Rule in section 93 by providing that one would look at whether an "*ordentlichen und gewissenhaften Geschaeftsleiter*" would

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<sup>61</sup> Assman, Lange and Sethe "Law of Business Associations" 154.

<sup>62</sup> Assman, Lange and Sethe "Law of Business Associations" 154.

<sup>63</sup> Section 111(4) of the *Aktiengesetz* (AG).

<sup>64</sup> See for example ss 77, 84, 90, 112, 118, 171, 172 and 179 of the AG.

<sup>65</sup> Section 111(5) of the AG.

<sup>66</sup> Section 116 of the AG.

<sup>67</sup> Section 93 of the AG and s 43 of the *Gesetz betreffend die Gellschaften mit beschränkter Haftung* (GmbHG) respectively.

<sup>68</sup> Spindler "§93 Sorgfaltspflicht und Verantwortlichkeit der Vorstandmitglieder" 544. Also see Alexander "GmbHG" 921.

<sup>69</sup> Alexander "GmbHG" 922. Also see Spindler "§93 Sorgfaltspflicht und Verantwortlichkeit der Vorstandmitglieder" 548.

<sup>70</sup> Ihrig and Schäfer *Rechte und Pflichten des Vorstands* 495.

<sup>71</sup> Ihrig and Schäfer *Rechte und Pflichten des Vorstands* 497.

have acted in the same way and also that there would be no breach of duty if the director, when making a business decision could rationally assume that on the basis of reasonable information that he was acting in the best interest of the company.<sup>72</sup> Although the liability in terms of section 93 is not delictual, the elements of a delict have to be satisfied.<sup>73</sup> The company would have to prove an act or omission, causation, and that the act caused loss. The director would have to show that the act that he committed, or the omission, was not a breach of duty, and he would have to prove that he had not been negligent.<sup>74</sup> There is therefore a presumption that the director has breached his duty of care and/or his fiduciary duty.<sup>75</sup> The director would therefore have a very difficult burden of proof to escape liability.

Very similar to the South Africa position seems to be the determination of whether the business judgement rule has been satisfied. The test is *ex ante* and not *ex post facto*. The question is whether the director made a rational decision which he thought was in the best interest of the company and which decision was based on objectively determined reasonable grounds.<sup>76</sup> It is not the intention to compare the German law with the South African in any detail, but only to indicate that the claim by the company against the director is not classified as delictual, although the elements that need to be proved are the elements that would have to be proved for a claim in delict. It is also important to bear in mind that the liability exists in conjunction with a contractual claim, for example. The crucial indicator would probably be the fact that for a breach to be present, the act had to be in respect of a business decision.<sup>77</sup>

From the perspective of the members of the supervisory board, the duty of care would entail that in respect of their supervisory, advisory and human resources duties, they should exercise those duties with the care and skill with which a reasonable and diligent supervisor, advisor or human

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<sup>72</sup> Ihrig and Schäfer *Rechte und Pflichten des Vorstands* 497; also see *Arag* decision of the BGH 21.4. 1997 II ZR 175/95. Section 93 of the AG states that "*Eine Pflichtverletzung liegt nicht vor, wenn das Vorstandsmitglied bei einer unternehmerischen Entscheidung vernünftigerweise annehmen durfte, auf der Grundlage angemessener Information zum Wohle der Gesellschaft zu handeln*".

<sup>73</sup> Ihrig and Schäfer *Rechte und Pflichten des Vorstands* 508-509.

<sup>74</sup> Hüffer *Aktiengesetz* 508.

<sup>75</sup> Spindler "§93 Sorgfaltspflicht und Verantwortlichkeit der Vorstandmitglieder" 601.

<sup>76</sup> See Habersack *et al* "Band 4/2 §§92-94" 157-158; Spindler "§93 Sorgfaltspflicht und Verantwortlichkeit der Vorstandmitglieder" 562 and Hüffer *Aktiengesetz* 500-502.

<sup>77</sup> See further Spindler "§93 Sorgfaltspflicht und Verantwortlichkeit der Vorstandmitglieder" 557 as well as Hüffer *Aktiengesetz* 500-501.



resources manager would have employed.<sup>78</sup> As said before, Keyay pleads for a clearer distinction for establishing breach by executive directors. The German provisions in respect of the supervisory board make more sense than the common law general provisions in respect of the duty of directors in general. Apples are compared with apples. One would determine whether the non-executive director exercised his duties with the necessary care and skill by comparing how he exercised his duties with how a reasonable and diligent non-executive would have done so. What is important, though, is not only the fact that the duties of the executive and the non-executives are differentiated but that the *sui generis* statutory liability (even if delictual elements are used) stands side by side with any contractual liability.<sup>79</sup>

## 5 An analysis of the basis of liability in South African law

Can contractual liability co-exist with delictual liability? It is clear that the wording of section 77(2)(b) cannot be correct. The Mol of the company clearly forms a contractual bond between the directors and the company. Although the rights and duties of directors are determined by a number of sources, as mentioned before, ultimately the wording of section 15(6) of the Act makes it clear that the directors are bound by the Mol.<sup>80</sup> The Act does not distinguish between executive and non-executive directors. Even if non-executive directors do not have employment contracts with the company, they are at the very least still bound by the Mol. It is also difficult to see how a non-executive director could be appointed to a board of directors without some form of agreement in place. It is therefore difficult to comprehend how a director could be held liable in delict where he breaches the provisions of the Mol. An argument could be that the elements of the delict have to be proved to prove breach of contract. Does this, however, exclude a concurrent contractual claim?

Let us first consider the duty of care and skill in more detail. As indicated above, the English courts were initially very lenient in holding directors liable for a breach of their duty of care and skill due to the subjective standard which was used. This was done because directors were seen as

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<sup>78</sup> Wellhöfer, Peltzer and Müller *Die Haftung von Vorstand Aufsichtsrat Wirtschaftsprüfer* 562.

<sup>79</sup> Section 116 of the AG.

<sup>80</sup> Cassim *et al Contemporary Company Law* 142 argues that the binding nature of the Mol may still be based on a statutory contract. Also see Delpont *et al Henochsberg on the Companies Act* 298(3)-299, who similarly argue that a contractual relationship is established by the Mol.

benevolent amateurs who provided status to the company and not necessarily for their business acumen.<sup>81</sup> The duty, even if now partially codified, remained delictual in nature but the argument still is that it should be read in the context in which it was developed; ie mainly in respect of those directors who acted as non-executive directors. When one considers most of the case law which has developed in respect of breach of duty of care and skill it would appear to be mainly cases where non-executive directors were sought to be held liable.<sup>82</sup>

Section 180 of the Australian *Corporations Act* also partially codifies the duty of care and skill of directors. Although it is not stated in the *Corporations Act*, the duty of care and skill lies in tort. The *Corporations Act* similarly imposes the duty on directors. In the definition of directors, no mention is made of a distinction between executive and non-executive directors. However, the *Corporations Act* does not specifically state what the basis of liability will be, unlike its South African counterpart where it is stated that the liability is to be determined in terms of the common law rules in respect of delict.

It is submitted that the Act should have remained silent about the delictual nature of the duty of care and skill because, as has been shown above, the basis of the duty is not necessarily delictual anymore. Executive directors are appointed with employment contracts which would set out their rights and obligations, and in most cases the common law and statutory duties would be implied terms of the contract of employment.<sup>83</sup> Also in respect of non-executive directors, their appointments as such would contain as implied terms that they would also act with the necessary care and skill in all matters. They are in any event also bound by the Mol of the company. This leaves the question whether the company could have a contractual claim against a director who breaches his duty of care and skill. Here the issue of concurrence of claims is important.

It has been mistakenly thought for over twenty years that a claim in contract would deny a claim in delict and *vice versa*. This mistaken belief

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<sup>81</sup> Bouwman 2009 SA Merc LJ 512 with reference to Havenga 2000 SA Merc LJ 34.

<sup>82</sup> *Daniels v Anderson* 1995 16 ACSR 607; *Fisheries Development Corporation; Re City Fire*; *Dorchester Finance Co Ltd v Stebbings* 1989 BCLC 498 (Chancery Division); and *Equitable Life Assurance Society v Bowley* 2004 1 BCLC 180; 2003 EWHC 2263 (Comm).

<sup>83</sup> See Naude *Regsposisie van die Maatskappydirekteur* 155-157, who argues that liability could be contractual, *ex lege* or delictual. Naude mentions that the advantage of contractual liability would be that different directors would have different duties in terms of their contracts and therefore one could look at the individual director's duty and whether this was breached.

was caused by an incorrect understanding of *Lillicrap, Wassenaar and Partners v Pilkington Brothers SA (Pty) Ltd*.<sup>84</sup> The case essentially held that there could be no delictual claim where the negligence which was complained about consisted of a breach of a contractual term.<sup>85</sup> However, Grosskopf AJA stated and approved of the following:

The same conduct may constitute both a breach of contract and a delict. This is the case where the conduct of the defendant constitutes both an infringement of the plaintiff's rights *ex contractu* and a right which he had independently of the contract.<sup>86</sup>

The court then continued and the statement which may have caused the confusion was the following:

In considering whether an extension of Aquilian liability is justified in the present case, the first question that arises, is whether there is a need therefor. In my view, the answer must be in the negative, at any rate in so far as liability is said to have arisen while there was a contractual *nexus* between the parties. While the contract persisted, each party had adequate and satisfactory remedies if the other were to have committed a breach. Indeed the very relief claimed by the respondent could have been granted in an action based on breach of contract. Moreover, the Aquilian action does not fit comfortably in a contractual setting like the present. When parties enter into such a contract, they normally regulate those features which they consider important for the purpose of the relationship which they are creating. This does not of course mean that the law may not impose additional obligations by way of *naturalia* arising by implication of law, or, as I have indicated above, those arising *ex delicto* independently of the contract. However, in general, contracting parties contemplate that their contract should lay down the ambit of their reciprocal rights and obligations. To that end they would define, expressly or tacitly, the nature and quality of the performance required from each party. If the Aquilian action were generally available for defective performance of contractual obligations, a party's performance would presumably have to be tested not only against the definition of his duties in the contract, but also by applying the standard of the *bonus paterfamilias*. How is the latter standard to be determined? Could it conceivably be higher or lower than the contractual one? If the standard imposed by law differed in theory from the contractual one, the result must surely be that the parties agreed to be bound by a particular standard of care and thereby excluded any standard other than the contractual one. If, on the other hand, it were to be argued that the *bonus paterfamilias* would always comply with the standards laid down by a contract to which he is a party, one would in effect be saying that the law of delict can be invoked to reinforce the law of contract. I can think of no policy consideration to justify such a conclusion.... It seems anomalous that the delictual standard of *culpa* or fault should be governed by what was contractually agreed upon by the parties....

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<sup>84</sup> *Lillicrap, Wassenaar and Partners v Pilkington Brothers SA (Pty) Ltd* 1985 1 SA 475 (A) (*Lillicrap*).

<sup>85</sup> Generally see the passage from *Lillicrap* 499A-501H.

<sup>86</sup> *Lillicrap* 499I with reference to Midgley and Van der Walt "Delict" para 53. Emphasis added.

*To sum up, I do not consider that policy considerations, require that delictual liability be imposed for the negligent breach of a contract of professional employment of the sort with which we are here concerned.*<sup>87</sup>

In *Pinshaw v Nexus Securities (Pty) Ltd*<sup>88</sup> a claim for pure economic loss caused by bad investments was lodged against the second defendant, a director of the first respondent, which in turn was sued for breach of contract based upon the allegation that it had acted in bad faith and dishonestly. The delictual claim against the second defendant was based upon gross negligence, recklessness and fraud. The court stated the following:

*Lillicrap's case (supra) was concerned with professional engineers rendering their professional services in terms of a contract with Pilkington Brothers and later in terms of a subcontract. In my respectful opinion, Lillicrap should not be extended to quasi-professionals, such as Nexus, offering financial services and holding themselves out, expressly or by implication, as possessing appropriate skills. Nor should Lillicrap be extended to the employees of such quasi-professionals. This is not to say that companies offering financial services, or their employees, will always attract a legal duty of care to their clients. That must depend on the circumstances. It is more than 15 years since Lillicrap was decided. The cases in this developing area of the law, in this country and elsewhere, do not indicate a need to extend the Lillicrap embargo to a broader class of defendants. On the contrary, the case law in my view supports the need to retain flexibility.*<sup>89</sup>

In *Holtzhausen v ABSA Bank Ltd*<sup>90</sup> the Supreme Court of Appeal cleared up the apparent confusion which the statements in *Lillicrap* had caused. The court stated, with reference to the above statement from the *Pinshaw* case that:

*Lillicrap (supra) is not authority for the more general proposition that an action cannot be brought in delict if a contractual claim is competent. On the contrary, Grosskopff JA was at pains to emphasise (at 496D–I) that our law acknowledges a concurrence of actions where the same set of facts can give rise to a claim for damages in delict and in contract, and permits the plaintiff in such a case to choose which he wishes to pursue.*<sup>91</sup>

And then further:

The court in *Pinshaw* erred in two respects. First, the premise underlying the reasoning is that *Lillicrap* decided that where delictual liability coexists with liability for breach of contract, the aggrieved party is limited to a claim in contract. That premise is wrong, as I have already shown. Second, the remarks of Grosskopff AJA in the passage just referred to reflect the facts of the case before the court which concerned a contract of professional

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<sup>87</sup> *Lillicrap* 500F-501H. Emphasis added.

<sup>88</sup> *Pinshaw v Nexus Securities (Pty) Ltd* 2002 2 SA 510 (C) (*Pinshaw*).

<sup>89</sup> *Pinshaw* 535F-I.

<sup>90</sup> *Holtzhausen v ABSA Bank Ltd* 2005 2 All SA 560 (SCA) (*Holtzhausen*).

<sup>91</sup> *Holtzhausen* 564 para 7.

employment, and must not be interpreted as limiting the principle laid down in that case to such contracts.<sup>92</sup>

It has been interesting to note that the confusion about the concurrence of claims has always seemingly been whether a delictual claim could exist besides the contractual claim. In respect of the breach of the duty of care and skill the question is the reverse, namely whether there is a contractual claim based upon the breach of contract besides the delictual claim, on the assumption that there is a delictual claim.

In *Daniels v Anderson*<sup>93</sup> the court stated that:

A director could be sued in equity, for a breach of fiduciary duty, and, in appropriate cases, *for breach of contract*, but not for unliquidated damages at common law in an action for negligence.<sup>94</sup>

As mentioned above, the *Daniels v Anderson* case, *Dorchester Finance v Stebbings*, *Equitable Life Assurance Society v Bowley* and locally the *Fisheries Development* cases all dealt with the liability of the non-executive directors in delict. This is probably understandable as argued already, because the executive directors would have employment agreements which would contain implied terms that they would not breach their duty of care and skill to the company.

From the perspective of the interpretation of statutes a few issues are important, namely particularly whether the seemingly clear wording of section 77(2)(b) in respect of delictual liability would exclude contractual liability. This would require some discussion of the interpretation of statutes. However, the aim is not to argue that interpretation rules should be used to interpret the relatively clear literal meaning of section 77(2)(b). The aim of this article is to show that the section has been incorrectly drafted.

However, it is arguable, since the common law has not been abolished by the codification of the directors' duties,<sup>95</sup> that in terms of the common law the company would still have a contractual claim against errant directors who breach their duties of care and skill and the MoI. It would be an unfortunate state of affairs, however, if the statutory position were delictual and the common law position were either delictual or contractual. In the

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<sup>92</sup> *Holtzhausen* 564-565 paras 9-10.

<sup>93</sup> *Daniels v Anderson* 1995 16 ACSR 607.

<sup>94</sup> *Daniels v Anderson* 1995 16 ACSR 607 655. Emphasis added.

<sup>95</sup> *Cassim et al Contemporary Company Law* 523 states that "the two sources [the Act and the common law] apply in parallel".

light of the fact that the business judgement rule is not part of our common law, the same argument would apply. It is therefore imperative that section 77(2)(b) be amended to remove the phrase "common law principles related to delict" and especially the phrase in respect of breach of the MoI. It would also be highly beneficial if the legislature recognised the clear distinction between the roles of the executive and the non-executive directors as in practice and in German law. This recognition does not have to have the abolition of the unitary board system as a consequence.

An important question, however, is what difference it would make whether liability is contractual or delictual in nature. The answer is especially important in the context of executive directors who are simultaneously employees of companies with employment contracts as well as the holders of the office of directors. Would one then have to determine in which capacity a director acted in order to be able to determine whether any claim which the company might institute against the director should be contractual or delictual? In many cases there is no clear distinction between these two roles of executive directors, and it would therefore be difficult to differentiate between them as a basis for liability. The question still remains whether a contractual claim would make any practical difference. If one departs from the hypothesis that the relationship between executive directors and the company is primarily contractual in nature, i.e. that there is an employment relationship, whereas the relationship and liability of non-executive directors is delictual, there is a very important practical consequence.

Loubser<sup>96</sup> argues that where there is a contractual relationship between parties and one of the parties brings a claim in delict, the standard of liability would generally be the same. In this light a statutory delictual claim that a director breached his duty of care and skill in respect of the fault requirement would be determined subjectively. A claim based on breach of contract would not therefore make the determination of breach strict, and conceivably breach of contract would be determined based on negligence, which would be determined subjectively. In terms of the common law, however, the basis of liability could be different. If one assumes that the relationship between an executive director and the company is primarily contractual, the basis of liability, even if negligence is required, would be

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<sup>96</sup> Loubser 1997 *Stell LR* 128-130. Although the article deals with the concurrence of contractual and delictual liability and the standard of liability from the perspective of an independent delictual claim where there is a contract between parties, the principle should be the same where the point of departure is delictual liability but a party wants to rely instead on a contractual claim.

the reasonable person test, and hence more objective in nature. A plaintiff company would therefore base its claim for breach of the duty of care and skill against an executive director on the common-law duty of care and skill, but specifically based in contract. This would be done to avoid the business judgement rule being raised, but also to avoid the confusion of the statutory use of the term "director". Even if there is no practical relevance at first blush, it is crucial that the common law and legislation should be clear about the nature of any claim.<sup>97</sup>

## 6 Conclusion

A few questions were posed in the introduction to this article. The first question was whether the legislature was correct to phrase the liability of directors in section 77(2)(b) of the Act as being delictual in nature. The second question was whether there are or should be different bases for liability depending on the director who is sought to be held liable. Thirdly it was asked whether it is correct that there should be different standards to determine the liability of executive directors and non-executive directors.

In respect of the first question it has been established that directors are bound by the Mol of a company. This means that there is some form of contractual bond between the company and the directors. A breach of the Mol by a director, whether executive or non-executive, is a breach of contract. The reference to delictual liability for a breach of the company's Mol cannot therefore be correct unless the intention of the legislature was that to determine breach of contract, the elements of a delict had to be present.

In respect of the duty of care and skill, it has been shown that the case law dealing with liability has mainly been in respect of non-executive directors. The cases and referenced works also established that the functions of the executive and non-executive directors are distinguished. It has been shown that traditionally non-executive directors were on the board only to provide prestige to the company, but that this role has changed. Non-executive directors play very important roles on boards in the modern era and are not benevolent amateurs anymore. They are bound by the provisions of the Mol and are also often appointed by some form of contract detailing their obligations. It is also clear that executive directors have employment contracts which set out their respective rights and obligations. Therefore to provide that the liability for a breach of the duty of

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<sup>97</sup> See generally Loubser 1997 *Stell LR* 128-140. Also see Loubser and Midgley *Law of Delict in South Africa* 189-195.

care and skill shall be determined according to the principles relating to delict is incorrect. The correct common-law position for executive directors is that the liability is contractual. It is arguable that the common law position for non-executive directors could also be contractual even if their appointments as such are not as employees but a *sui generis* type of appointment. Our law after *Lillicrap* and *Holtzhausen* recognises a concurrence of delictual and contractual claims. In the light of the fact that the common law co-exists with the Act, it would certainly not be advisable that liability in terms of the Act should differ from liability in terms of the common law. It is therefore strongly suggested that the phrase in section 77(2)(b) of the Act which refers to delictual liability should be removed.

The last question which was posed was whether it is correct that there are different standards of liability on the assumption that the non-executive directors are liable in delict. It has been shown that the role of non-executive directors has changed and that they do have some form of appointment letters setting out their duties, which are supervisory in nature. Any breach of these duties would constitute a breach of a very specific type of contract. If, however, it is maintained that the liability is delictual, a clearer distinction should be made in legislation between executive and non-executive directors, as pleaded for by Keay. This distinction is clear in German law. This does not, however, have to lead to a two-tier system. A unitary board could still be maintained, but with clear legislative guidelines in respect of the different roles of the directors. A determination in respect of liability for breach of the duty of care and skill can then be made much more easily, and the determination of liability for non-executive directors would be based on the supervisory duties of such directors. It is still arguable, however, that all directors are essentially liable in contract and possibly still in delict, that a concurrence of actions is possible in terms of our common law, and that the Act should correctly reflect this instead of incorrectly stating that the liability of directors for breaches of the Mol and the duty of care and skill is delictual. The standard to determine breach of contract may be important, however, when one argues that the duties of executive directors have (always) been contractual in the common-law and that, should fault be required, the common-law breach of contract would be more objective in nature.



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### **List of Abbreviations**

|            |   |
|------------|---|
| AG         | Aktiengesetz  |
| FRC        | Financial Reporting Council                                 |
| BGB        | German Civil Code   |
| GmbH       | Gesetz betreffend die Gellschaften mit beschränkter Haftung |
| IoD        | Institute of Directors (UK)                                 |
| IoDSA      | Institute of Directors in Southern Africa                   |
| Mol        | Memorandum of incorporation                                 |
| NPC        | Non-profit company  |
| Nw UL Rev  | Northwestern University Law Review                          |
| SA Merc LJ | South African Mercantile Law Journal                        |
| Stell LR   | Stellenbosch Law Review                                     |