A SOUTH AFRICAN PERSPECTIVE: THE MODERN COMPANY AND CORPORATE GOVERNANCE IN THE COMPANIES ACT 2008.

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I INTRODUCTION

South African company law has transformed since its inception under the Joint Stock Companies Limited Liabilities Act[1] (herein after referred to as 'the Joint Stock Act') to its current form under the Companies Act[2] (herein after referred to as 'the 2008 Act'). This transformation was necessitated by various changes, such as globalisation, interconnected trade, and a greater emphasis on oversight, management and accountability in company law practice.[3] Additionally, the propositions made by the South African Department of Trade and Industry (DTI) around the need to modernise the company law framework, and to create stronger and more effective rules around corporate governance, contributed to this radical transformation.[4] This transformation process is especially significant when examining corporate governance and the need to ensure ethical and sustainable company law practices.

The main focus of this research report will be analysing the role of corporate governance in contemporary South African company law by identifying the relationship between the two, and understanding how one can be used to better enhance the other. In undertaking this analysis, it is important to understand what is meant by the term 'corporate governance'. Cassim defines corporate governance, in the narrow sense, as '…the structures and processes associated with management, decision-making and control in organisations'.[5] In other words, corporate governance comprises of a management system pertaining to the (appropriate) conduct of directors and managers, and the discharging of their duties to the company and its shareholders accordingly.[6] Cassim further defines a wider sense of corporate governance as that which comprises effective, responsible, ethical,

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[1] Act 23 of 1861.

[2] Act 71 of 2008.

[3] The Government Notice GN 1183GG26493 of 23 June 2004. See also Farouk H.I. Cassim, Maleka Femida Cassim, Rehana Cassim, Richard Jooste, Joanne Shev & Jacqueline Yeats *Contemporary Company Law* 2 ed (2017) at 473 where it is said that '[i]n recent years a series of highly publicised corporate scandals and high profile corporate failures worldwide have prompted the further development of corporate governance principles and practices, and have highlighted the lack of effective accountability within companies'.

[4] Ibid.

[5] Cassim et al op cit note 3 at 472. See also Tom Wixley & Geoff Everingham, *Corporate Governance* 3 ed (2010) at 1.

[6] Ibid at 473.

accountable, fair and transparent leadership (so-called good corporate governance).[7] In the *Stilfontein* case,[8] Hussain J stated that good corporate governance is a necessary company law practice because it is essential for the company's well-being, and to the growth of the South African economy especially from the perspective of securing investments.[9] Good corporate governance can also attract a better calibre of employees which in turn feeds the cycle of profit and growth in the company and the economy.[10]

For purposes of this research report, the wider sense of corporate governance (the good corporate governance aspect) shall be emphasised with a focus largely on the need for directors (and shareholders, but my emphasis is on the former) to ensure compliance with section 7 of the 2008 Act. Thus, section 7 serves as a pivot around which I will be arguing for good corporate citizenship and the need for stronger stakeholder inclusivity within this framework.

First, I highlight the evolution of the company from what was a rather archaic entity to a more modern one that is better suited to its current economic and social context. In doing so, the purposes of the company under section 7 shall become apparent. I will further analyse the broad nature of section 7. This will in turn contextualise the new company law era under the 2008 Act.

Secondly, I consider in whose interest the company should be run, and I outline the debates and theories in company law surrounding this question. These theories include the shareholder-centric approach; the pluralist or stakeholder approach; and the enlightened shareholder-value approach. In each respect, the main propositions and criticisms will be discussed.

Thirdly, I examine what is meant by the director's fiduciary duty to act in 'the best interests of the company' under section 76(3)*(b)* of the 2008 Act. I further explore the public company in a modern context and the statutory requirement of a social and ethics committee in the 2008 Act. While directors bear the fiduciary duty of acting in the best interests of the company and its shareholders under section 76(3)*(b)*, a closer and analytical consideration of the 2008 Act in its entirety gives a broader injunction for directors to consider other stakeholders too. This accords with the 'triple bottom line approach' which is the inclusion of economic, social and environmental concerns as outlined in the King III Report, and the strong emphasis on stakeholder inclusivity in the King IV

[7] Ibid. See also *South African Broadcasting Corporation Ltd v Mpofu* 2009 4 All SA 169 (GSJ) para 64 in which the court held that '…good corporate governance is based on a clear code of ethical behaviour and personal integrity exercised by the board, where communications are shared openly'.

[8] *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company Limited* 2006 ZAGPHC 47.

[9] Ibid para 16.7. See also John Plender 'Shareholders are being dethroned as rulers of value' available at *https://www.ft.com/content/42871952-0463-11e9-99df-6183d3002ee1*, accessed on 2 January 2019 in which he explains that investors are increasingly more focused on 'environmental, social and governance factors' in business.

[10] Ramani Naidoo *Corporate Governance: An Essential Guide for South African Companies* 2 ed (2009) at 10.

Report.[11] While the King Reports are not binding in nature, they are persuasive and useful for courts. In order to give effect to the broadly drafted purposes of section 7 of the 2008 Act, such as 'reaffirm[ing] the concept of a company as a means of achieving economic and social benefits',[12] it would be unwise to consider the King Reports as irrelevant merely because the reports are of a non-binding nature.

In assessing the strengths and weaknesses of each theory, I propose a balanced and holistic approach that takes into account the circumstances and context of the company; the 2008 Act; and the King Reports to better enhance the enlightened shareholder-value approach, and to be more inclusive of stakeholder interests without placing profit maximisation on the back-burner.

II SETTING THE CONTEXT: THE DEVELOPMENT OF THE MODERN COMPANY

It is necessary to consider the progression of the company in South Africa from its colonial past to its current manifestation in the 2008 Act. One of the results of British colonial rule in South Africa was that company law was shaped and influenced by English law to a large extent.[13] Thus, in 1861, South Africa enacted the Joint Stock Act[14], which was the first statutory piece of company law in South Africa .[15] This piece of legislation, in conjunction with the provincial enactments, very closely resembled English legislation.[16] In 1926, the Union of South Africa Companies Act[17] was enacted, and thereafter replaced by the Companies Act[18] (herein after referred to as 'the 1973 Act').[19] It is worth noting that while the 1973 Act largely bears its English law foundations, it is '…hailed as cutting the umbilical cord between the South African and English company law'[20] because of its more overt departure from English company law as compared to its predecessors.[21] Moreover, the 1973 Act was viewed as the 'last extensive reform of company law'[22] (that is, until the 2008 Act was

[11] Institute of Directors in Southern Africa (IODSA) 'King IV: Report on Corporate Governance for South Africa 2016' available at *http://www.iodsa.co.za*, accessed on 10 June 2018.

[12] Section 7(d) loc cit note 2.

[13] Government Notice loc cit note 3.

[14] Act 23 of 1861 loc cit note 1.

[15] Government Notice loc cit note 3.

[16] Ibid.

[17] Act 46 of 1926.

[18] Act 61 of 1973.

[19] Government Notice loc cit note 3.

[20] Ibid.

[21] Ibid. However, it is important to note that the DTI considered the Close Corporations Act 69 of 1984 as the most significant departure from English common law in that it introduced an entirely new way in which small companies could be incorporated.

[22] Ibid.

enacted) despite being modelled off its 1926 predecessor.[23] This signifies the extent to which the 2008 Act has reformed company law as compared to the 1973 Act, which itself was viewed as an extensive reform.

However, as economies around the globe began changing so too did the local environments in which companies operated. Thus, in 2004, the DTI reviewed the 1973 Act.[24] At the time, the 1973 Act was thirty years old and it was clear that serious reforms needed to be made in order to better reflect the business climate of the time.[25] For example, the concept of globalisation and interconnected trade and business had already emerged in the 1970s and was well underway by 2004.[26] Moreover, there seemed to be an underlying fear expressed by the DTI on the slow-to-change company law regime within the domestic realm itself:

> 'South Africa cannot afford to be left behind. There is a growing recognition by companies and governments that there is a need for higher standards of corporate governance and ethics and greater interdependence between enterprises and the societies in which they operate…Socio-political and economic change in South Africa has underscored the need for social responsiveness, transparency and accountability of enterprises'.[27]

This fear came largely due to the fact that 1973 Act had not seen any dramatic changes as a whole since its inception despite having been amended numerous times.[28] It can be argued that various factors, such as the 'highly formalistic…burdensome and costly'[29] formation and management of a company, coupled with the sense of stagnation around the 1973 Act, contributed to the enactment of the 2008 Act.[30] Other factors more relevant to this research report include South Africa's democratic birth in 1994 and, of more legal significance, the enactment of the Constitution of the Republic of South Africa, 1996 (herein after referred to as 'the Constitution').[31] The Bill of Rights in Chapter 2 of the Constitution added an extensive human and rights-based element to the South African legal system as a whole.[32] It must then be asked – what did this mean for company law? As a starting point, company law now needed to be consistent with the Constitution and its values and purposes.[33] An

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[23] Ibid.

[24] Ibid. See also Rehana Cassim & Femida Cassim 'The Reform of Corporate Law in South Africa' 2005 *International Company and Commercial LR* 411 at 411.

[25] Ibid.

[26] Ibid.

[27] Ibid.

[28] Cassim et al *Reform* op cit note 24 at 411. See also Farouk H.I. Cassim 'The Companies Act 2008: An Overview of a Few of its Core Provisions' (2010) 22 *SA Merc LJ* 157 at 157.

[29] Government Notice loc cit note 3.

[30] Ibid.

[31] Ibid.

[32] Ibid.

[33] Ibid.

element of harmonisation between the different pieces of legislation had become necessary in law.[34] Of course, as shall be discussed further below, this form of harmonisation has now been achieved via section 7(a) of the 2008 Act.[35]

However, harmonisation itself would not suffice – the company would need to become more modern to fit a contemporary context.[36] This view has been expressed by Cassim et al in that there was a strong need to abandon outdated company law concepts in order to better align South African company law with its modern context and international business practices.[37] While a large part of the modernisation of company law would come in the form of making company formation less costly and time-consuming,[38] the laws regulating corporate governance and the duties and liabilities of directors needed to be made more apparent.[39] The common law served as a primary source of law in this respect, and it continues to be relevant in the 2008 Act as shall be discussed further below.[40] The DTI's concern was that the 1973 Act did not adequately provide for effective mechanisms to enforce directors duties, thus causing executive management and directors of large companies to be 'immune from legal control'.[41] This was particularly apparent from the absence of a public institution with the powers and resources to investigate and enforce the rights of shareholders and other stakeholders.[42] Thus, not only did issues of corporate governance come to the forefront, but the question of where stakeholders fit into the company law framework arose on the topic of corporate governance. Significant debates and theories exist on this question as shall be discussed further below.[43]

Essentially, the DTI had expressed a tectonic shift in the company law landscape from the very technical elements of a company, such as its formation, towards the more substantial elements, such as its objectives and purposes. Furthermore, it was emphasised that companies ought to take into account the role which they play in the South African economy and identify any challenges so as to stimulate development and competitiveness.[44] The DTI proposed that growth could be achieved by making company formation simpler and cheaper to enhance entrepreneurial opportunities; to provide companies with flexible formation and management as well as certainty and strong regulations for

[34] Ibid.

[35] This section promotes company law compliance with the Bill of Rights in the Constitution and is discussed in section III below.

[36] Government Notice loc cit note 3.

[37] Cassim et al *Reform* op cit note 24 at 411.

[38] Ibid. See also GN loc cit note 3.

[39] Ibid.

[40] Ibid. See also sections IV & V below.

[41] Ibid.

[42] Ibid.

[43] See section IV below.

[44] Government Notice loc cit note 3.

purposes of innovation and investment in the market; to promote the efficiency of companies; to promote a sense of transparency and accountability by strengthening corporate governance rules whilst also *'recognising the broader social role of enterprises'*;[45] and to provide for harmonisation and compatibility with international jurisdictions which serve as model jurisdictions for South Africa (my emphasis).[46] These were dubbed the 'five pillars of the DTI policy paper'.[47] The inclusion of section 7 of the 2008 Act – the provision containing the purposes of the new Act – echoes the sentiments contained in the five pillars of the DTI policy paper.

III A NEW COMPANY LAW LANDSCAPE: SECTION 7 OF THE 2008 ACT

Section 7 includes in its purposes the application of company law in compliance with the Bill of Rights in the Constitution;[48] developing the South African economy by way of encouraging and enhancing entrepreneurship, flexible and simple formation and management of the company, and providing for transparency with high standards of corporate governance '…given the significant role of enterprises within the social and economic life of the nation';[49] and to '…reaffirm the concept of the company as a means of achieving economic and social benefits'.[50] For purposes of this research report, these provisions are directly relevant to the arguments I will be making.

Other purposes include promoting innovation and investment in the markets;[51] using the company so as to enhance economic welfare of South Africa as a means to participate in the global economy;[52] developing the company in all sectors of the economy;[53] creating conditions conducive to capital investment;[54] regulating non-profit companies in terms of its formation, operation and accountability;[55] balancing the rights and obligations of shareholders and directors in a company;[56] encouraging the efficient and responsible management of the company;[57] providing for efficient business rescue procedures taking into account relevant stakeholder rights and interests;[58] and

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[45] Ibid.
[46] Ibid.
[47] Cassim *Overview* op cit note 28 at 158.
[48] Section 7(a) loc cit note 2.
[49] Ibid s7(b)*(i)-(iii)*.
[50] Ibid s7(d).
[51] Ibid s7(c).
[52] Ibid s7(e).
[53] Ibid s7(f).
[54] Ibid s7(g).
[55] Ibid s7(h).
[56] Ibid s7(i).
[57] Ibid s7(j).
[58] Ibid s7(k).

providing a predictable and effective regulation of companies.[59] At face value, section 7 clearly indicates that the company is not an entity that can be separated from corporate governance structures and the broader society and economy in which the company exists.

In understanding the link between the purposes of the 2008 Act and corporate governance, the relevance of section 7 to corporate governance must be examined. To this end, it is useful to analyse the nature of section 7 and the manner in which it operates in the 2008 Act. Its relevance can be ascertained on a mere reading of section 7(b)*(iii)* in that it contains an express reference to corporate governance. It can be argued that the inclusion of sections 7(b)*(iii)* and (d) firmly entrenches corporate governance as a concept and principle at the very onset of the 2008 Act.

The nature of section 7 and the manner in which it operates is explained as follows: section 5 of the 2008 Act – the general interpretation provision – states that '[the 2008 Act] *must* be interpreted and applied in a manner that gives effect to the purposes set out in section 7' (my emphasis).[60] The word 'must' implies a mandatory rather than a discretionary or optional task. Section 5(1) adds a weightier foundation to the broad and widely defined purposes set out in section 7.[61] Indeed, as Katzew states, '…the foundation [via section 5(1)] is laid for a purposive interpretation of the [2008] Act'.[62] In fact, the 2008 Act goes so far as to include '[r]emedies to promote purpose of Act' in section 158:

> 'When determining a matter brought before it in terms of this Act, or making an order…in this Act – (a) a court must develop the common law as necessary to improve the realisation and enjoyment of rights established by this Act; and (b) the Commission, the Panel, the Companies Tribunal or a court – (i) *must promote the spirit, purpose and objects of this Act*; and (ii) if any provision of this Act, or other document in terms of this Act, read in its context, can be reasonably construed to have more than one meaning, *must prefer the meaning that best promotes the spirit and purpose of this Act*, and will best improve the realisation and enjoyment of rights (my emphasis).'

The inclusion of a provision of this nature persuades one to believe that section 7 was not drafted for decorative purposes nor was it drafted for the sake of simply appearing as though the 2008 Act seeks radical change from its 1973 predecessor (which itself did not contain a purposes or objectives provision with its own interpretation and remedies provisions). This would further imply that the principle of corporate governance, as contained in section 7(b)*(iii)*, has also not been included merely for the sake of it, but rather as a principle that ought to be given effect to in the 2008 Act and

[59] Ibid s7(l).

[60] Ibid s5(1).

[61] Cassim *Overview* op cit note 28 at 159.

[62] Judith Katzew 'Crossing the Divide between the Business of the Corporation and the Imperatives of Human Rights - The Impact of section 7 of the Companies Act 71 of 2008' (2011) 4 *SALJ* 686 at 689.

in company law practice generally.

However, section 7, read with section 5(1), has been met with criticism. A main concern raised by Cassim is the question of how the courts are, in actuality, to give effect to the 'impossibly wide objectives'[63] contained in section 7.[64] Cassim does, however, recognise

> '[t]he fact that a statutory provision is inconvenient or absurd does not permit a court to ignore it if it is otherwise clear and unambiguous. The objectives or purposes set down in s 7 are prefatory and must remain so.'[65]

It would appear from this statement that section 7 is to be treated as a preamble of sorts that is persuasive in nature rather than a binding set of objectives to be achieved in the usual interpretation of company law. It is worth noting that this perspective, including the assertion that section 7 is overbroad, bears validity especially when considering that there is hardly any precedent in the new company law dispensation that places a large amount of emphasis on section 7 (this despite the assertion in section 5(1) of the 2008 Act as outlined above).[66] Of course, this may be as a result of the fact that, at the time of writing this paper, the 2008 Act is still a fairly new piece of legislation, but it is also likely as a result of the practical difficulty in giving effect to provisions that envision a fundamentally new company law landscape than the 1973 Act, for example. Thus, an interpretive danger exists – how far is too far? For example, if the courts were to give effect to and interpret section 7(d), as outlined above, the courts would be doing so in the absence of legal guidelines as to what exactly is meant by the elements contained in this provision. While it could create room for the courts to begin defining the elements in section 7, it could also result in the courts extending their judicial powers and functions and thus over-stepping the company law boundary in what is usually entrusted to the expertise and discretion of directors. This point must be emphasised as it has been contended that the courts should be reluctant to step into the shoes of the directors and make deliberations on their behalf..[67]

It appears that the only unambiguous purpose is found in section 7(a). This is largely owing to the fact that this provision expressly refers to the extensive Bill of Rights in the Constitution. The

[63] Cassim *Overview* op cit note 28 at 159.

[64] Ibid.

[65] Ibid.

[66] See for example *Venter v Silver Lakes Homeowners Association NPC* 2017 ZAGPPHC paras 7 & 9 in which De Villiers AJ outlines section 5(1) and section 7(a), but makes no ruling as to its applicability because it had not been pleaded by the parties.

[67] See *Re Smith & Fawcett Ltd* 1942 (Ch) 304 at 306 where the court explained that the duty to act in the interests of the company is a power conferred on the directors and what they deem to be in the interests of the company, and not a power conferred on the courts.

inclusion of this provision has been regarded as a rather 'bold move'[68] given the express will to integrate the discipline of company law with the rights and duties contained in the Constitution which were otherwise thought to be separate disciplines altogether.[69] Section 7(a) gives effect to section 8(1) of the Constitution, which provides that '[t]he Bill of Rights applies to all law…'.[70] Section 7(a) further gives effect to section 8(2) of the Constitution, which provides that a provision in the Bill of Rights binds natural and juristic persons, and that the provision in the Bill of Rights is applicable to the extent that it is appropriate in terms of the nature of the right and its corresponding duty.[71]

Katzew highlights the crucial point that there is a proviso contained in section 8(2) of the Constitution.[72] This proviso is described as 'the very crux of the difficulty in attributing human rights obligations to companies'[73] largely because it is not made clear in section 8 of the Constitution how the courts should determine the extent and nature of the right or duty in question.[74] However, Katzew further argues that section 7(a) does not itself contain such a proviso, thus leaving open to interpretation whether a 'more comprehensive and less ambiguous'[75] provision than that of section 8(2) of the Constitution was in fact intended in the 2008 Act.[76] Yet it is difficult to imagine that section 7(a) was intended to be 'more comprehensive and less ambiguous'[77] than section 8(2) of the Constitution. This is especially so when section 7(a) requires compliance with the Constitution. Nevertheless, section 7(a) and its express inclusion of the Bill of Rights in the Constitution seems to require that human rights and socio-economic factors are to feature prominently in the making of company policy.[78]

The emphasis on social responsibility and corporate governance in section 7(b)*(iii)* and (d) has not yet been considered by the courts and their impact is thus still unknown. It is, however, evident from a reading of section 7 in its entirety that there exists the purpose of profit maximisation as well as the recognition of a more human and social element as it relates to company law.[79] It is worth noting that the latter sentiments are perhaps expressed to a far lesser degree than the profit motive in

[68] Manson G. Gwanyanya 'The South African Companies Act and the Realisation of Corporate Human Rights and Responsibilities' (2015) 18(1) *PELJ* 3102 at 3107.
[69] Ibid.
[70] Katzew op cit note 62 at 690.
[71] Ibid.
[72] Ibid.
[73] Ibid.
[74] Ibid.
[75] Ibid.
[76] Ibid.
[77] Ibid.
[78] Ibid at 686-87.
[79] Ibid at 689.

general. Nevertheless, this seems to suggest some degree of shifting away from the traditional shareholder-centric approach in company law.[80] This prompts the very core question on which this research report is premised: in whose interest should the company be run?

IV THEORIES AND DEBATES: IN WHOSE INTEREST SHOULD THE COMPANY BE RUN?

In its policy paper, the DTI considered that the process of company law reform always begins with this 'fundamental question'.[81] This question essentially translates to whether directors, who are generally tasked with the management and oversight of the company,[82] are to act solely for the benefit of their shareholders, or whether broader interests are to be considered (such as the interests of other stakeholders).[83] Stakeholders, other than shareholders, include the company's employees; creditors; customers; suppliers; and it also includes environmental needs and the local community in which the company is situated.[84]

(i) The shareholder-centric approach

The DTI was not the first to consider this question. There are arguments surrounding this key question in English common law.[85] The general principle under English common law is that directors are under an obligation to act with honesty and in the interests of the company.[86] It must, however, be asked what comprises the 'company' as it relates to directors acting in the company's interest or for the company's benefit.[87] The 'benefit of the company' has been defined as 'the long-term interests of members [read as shareholders] as a whole'.[88] There are two main points to highlight here – first, the 'company as a whole' refers to the fiduciary duty owed to the collective body of shareholders rather than individual shareholders,[89] and secondly, it is not only the long-term interests of shareholders that are relevant, but also the short-term interests of shareholders.[90] This accords with the traditional shareholder-centric approach.[91] The DTI has mentioned three main theoretical underpinnings of this

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80 Ibid at 691.

81 Government Notice loc cit note 3.

82 See s66(1) loc cit note 2.

83 Government Notice loc cit note 3.

84 Cassim et al op cit note 3 at 517.

85 See generally Paul L. Davies & L.C.B. Gower *Gower's Principles of Modern Company Law* 7 ed (2003) at 479-87 for an understanding of how the English common law deals with the question of in whose interests the company should be run.

86 Government Notice loc cit note 3.

87 Brian Peter Lee Jennings 'Are Shareholders Exclusive Beneficiaries of Fiduciary Obligations in South Africa? The Role of Fiduciary Obligations in the 21st Century' (2015) 2 *JCCL&P* 54 at 56.

88 Government Notice loc cit note 3. See also *Percival v Wright* 1902 2 (Ch) at 421.

89 *Coronation Syndicate Ltd v Lilienfeld* 1903 TS 489.

90 Jennings op cit note 87 at 57.

91 Government Notice loc cit note 3. See also *Percival's* case supra note 88.

approach, namely –

> '(i) It is the shareholders who invested their capital in the company and so they are entitled to its profits after other claims are satisfied; (ii) The shareholders, as residual claimants of whatever is left over after all other claims have been paid, are best positioned to police the efficiency of the company; and (iii) The survival and economic success of a company will deliver social benefits to many stakeholder constituencies, which will not be delivered if the company is a financial failure.'[92]

Thus far, the position on stakeholders was articulated by the principle in the *Hutton* case where it was held that the test is not solely whether the action is carried out in good faith, but whether the action is also reasonably incidental to the carrying on of the company's business for its own benefit.[93] This is best expressed by the court's use of the analogy of 'cakes and ale' – that is, the company can enjoy profits and giving back to society as long as both profit-making and the company's exercise of goodwill are for the ultimate benefit of the company.[94] The court in the *Evans* case further upheld this principle in respect of charitable donations given by the company.[95] This legal principle places a restriction on the director such that he may only act in the public interest to the extent that it is beneficial for the company. Whether 'beneficial' is interpreted to mean profitable, or a financially sound decision at the very least (such as avoiding debt), is unclear. Nevertheless, this makes logical sense since directors are essentially entrusted with 'corporate funds that do not belong to them',[96] thus the question has been raised whether directors should be allowed to act in the public interest at all.[97]

Esser considers some of the arguments in favour of the shareholder-centric approach.[98] Such arguments include that shareholders are the "owners" of the company's assets and are deserving of 'exclusive protection',[99] and that shareholders are not protected by legislation in the same way in which the broader stakeholders are (for example by means of labour laws, insolvency law and consumer protection laws).[100]

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[92] Ibid. See also Trevor S. Norwitz 'The Metaphysics of time: A Radical Corporate Vision' (1991) 46 *Business Lawyer* 377 at 377.

[93] *Hutton v West Cork Railway* 1883 (ChD) at 654.

[94] Ibid at 672-3.

[95] *Evans v Brunner Mond & Company Ltd* 1921 (ChD) at 359. See also Cassim et al op cit note 3 at 517.

[96] Ibid.

[97] Ibid.

[98] Irene-Marie Esser & J.J. Du Plessis 'The Stakeholder Debate and Directors' Fiduciary Duties' (2007) 19 *SA Merc LJ* 346 at 358.

[99] Ibid at 359.

[100] Ibid.

(ii) The debate between Berle and Dodd

In the 1930s, a well-known debate arose between Professors Berle and Dodd on whether the company should be strictly shareholder-centric.[101] On the one hand, Berle believed that the sole purpose of making a profit for the company meant that directors' duties are to be exercised solely for the shareholders since "corporate powers [and the responsibility of directors] should be regarded as 'powers in trust'"[102] for the benefit of the shareholders.[103] Berle contended that, in the absence of 'a clear and reasonably enforceable scheme of responsibilities to someone else [other than directors]',[104] the notion that companies exist also for socio-economic purposes (as proposed by Dodd,[105] which is outlined in more detail below) is not a sound argument.[106] Essentially, Berle's viewpoint on stakeholder interests is premised mainly on the fact that he considered it unsafe and unsound for a corporation to be accountable to stakeholders in the absence of legal checks and balances to this effect.[107]

On the other hand, Dodd disagreed that the only purpose of the company is to make a profit for the company's shareholders or that the company has no responsibility towards social reform.[108] Dodd looked beyond profit maximisation and thought the company to be an '…economic institution performing a social service as well as a profit-making function'.[109] Dodd sustained this argument by asserting that the socio-economic function of a company had already, at that time, impacted legal theory and, Dodd further contended, that this would probably continue to impact future legal theory in a substantial way.[110] In fact, Dodd's perspective is in stark contrast to Berle's perspective in that Dodd argued that companies ought to account for 'broad social interests'[111] even where this diminishes shareholder interests.[112] This proposition is rather radical from the lens of shareholder-centrism, but, interestingly, the first companies that were incorporated in the United States were incorporated for public welfare purposes, such as providing water or transport to the community.[113]

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[101] Cassim et al op cit note 3 at 518.
[102] Katzew op cit note 62 at 692.
[103] Ibid.
[104] A.A. Sommer Jr 'Whom Should the Corporation Serve? The Berle-Dodd Debate Revisited Sixty Years Later' 1991 16 *Delaware J of Corporate Law* 33 at 37.
[105] Ibid.
[106] Ibid.
[107] E. Merrick Dodd Jr 'For Whom Are Corporate Managers Trustees?' 1931-32 *Harv LR* 1145 at 1372. See also Cassim et al op cit note 3 at 518.
[108] Ibid.
[109] Ibid. See also Dodd Jr op cit note 107 at 1147-8.
[110] Sommer Jr op cit note 104.
[111] Ibid at 54.
[112] Ibid.
[113] Ibid at 36.

This begs the question of whether Dodd's perspective was radical or simply a reminder of the underlying purpose for which companies were developed arguably for the benefit of the community in which the company exists.

An interesting occurrence was that Berle had later conceded, or so it seemed, to Dodd's view mainly owing to the fact that 'social fact and judicial decisions'[114] supported Dodd's contentions.[115] This debate continues to be relevant in the twenty-first century given the modern climate in which the company now exists. This is especially so where the need to make a profit has, at times, clashed with stakeholder interests, and consequently affected the company's long-term profit-making and investment opportunities,[116] as was the case in the Lonmin Mine and the Marikana massacre, for example, where Ndlovu argues that the Marikana incident was as a result of capital (that is, profit) versus labour (or employees who are stakeholders of the company).[117] In this instance, the sole focus in ensuring that the company remained productive and profitable for the benefit of the shareholders resulted in a failure to address the concerns of employees which proved to be detrimental to the short and long-term interests of the company.[118] Hence, emphasis must be placed on the legal principle in the *AP Smith Manufacturing* case, as it is an example of how judicial decisions have considered the socio-economic responsibility of companies, in which the court held that modern conditions demand that companies acknowledge and discharge their social and private responsibilities since the company, as a juristic person, also constitutes a member of the community in which it operates and thus bears a duty to its community.[119]

(iii) The pluralist or stakeholder approach

The principle in the *AP Manufacturing* case outlined above may go so far as to lead to the pluralist or stakeholder approach.[120] In this approach, the company is conscientious in that it accounts for social and environmental concerns when conducting its business activities whilst also engaging in

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[114] Ibid at 38.

[115] Dodd Jr op cit note 107 at 1156.

[116] Cassim et al op cit note 3 at 518.

[117] Morgan Ndlovu 'Living in the Marikana world: The state, capital and society' (2013) 8:1 *International Journal of African Renaissance Studies* 46 at 54.

[118] Peter Leon 'The mining industry after Marikana' available at *http://www.politicsweb.co.za/news-and-analysis/the-mining-industry-after-marikana*, accessed on 26 August 2018 in which the author mentions that 'One consequence of last year's labour unrest was a ZAR12 billion fall in mine production and a half a per cent decline in gross domestic product…Continuing labour unrest has contributed to a 5,4 per cent year-on-year decrease in mining production from June 2012 to June 2013…This decline in production continues to reflect the tough business conditions in a sector beset by labour issues, uncertain commodity prices and rising production costs'.

[119] *AP Smith Manufacturing Co v Barlow* 1998 A2d 581 (NJ 1953) at 586.

[120] Cassim et al op cit note 3 at 518.

solution-building with relevant stakeholders.[121] This approach views shareholders as another stakeholderfor directors to consider alongside the various other stakeholders.[122] In fact, *if the interests of company demand it*, the pluralist approach argues that directors ought to prefer stakeholder interests as a whole over shareholder interests alone (my emphasis).[123] This is further supported by Sommer Jr where it is argued that '…directorial attention should be [stakeholders] and not just stockholders'.[124]

Furthermore, the stakeholder approach takes into account the 'competing demands'[125] faced by the modern company on a daily basis, in the narrow sense, by their employees; customers; suppliers; creditors, and more broadly, by the local community; national interest; the economy and the environment in which the company operates.[126] The stakeholder approach is then best understood such that directors ought to be concerned with the interests of the company as a whole, which is broader than the shareholders alone, as this would more accurately reflect the demands of the modern company.[127] This approach is a significant departure from shareholder-centrism.

Naturally, the stakeholder approach is not without criticism. Academics, such as Jennings,[128] have gone so far as to call the approach 'unworkable'[129] in the absence of 'some system of legally ordered priorities between the different groups'.[130] This seems to reiterate Berle's view of an 'unchecked'[131] and 'unsafe'[132] approach, as outlined above.[133] Therefore, a crucial concern arises as to how one would go about positively enforcing a duty of this nature.[134] It has, however, been proposed that legislation, such as amending the 2008 Act to incorporate guidelines, can serve as a solution to address the issue ofhow such an approach may be enforced .[135] Whether or not this is an appropriate solution remains to be seen.

Secondly, it has been argued that the general body of stakeholders do not enjoy the same 'privity of contract' as shareholders do since '[c]reditors deal with a company as a matter of bargain,

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[121] Ibid.
[122] Ibid.
[123] Cassim et al *Reform* op cit note 24 at 411-12.
[124] Sommer Jr op cit note 104 at 38.
[125] Jennings op cit note 87 at 58.
[126] Ibid.
[127] Ibid.
[128] Ibid.
[129] Ibid.
[130] Ibid.
[131] Dodd Jr op cit note 107 at 518.
[132] Ibid.
[133] Ibid.
[134] Jennings op cit note 87 at 58.
[135] Ibid.

not of trust, and bargain involves risk'.[136] (It is interesting to note that this view is in stark contrast with one of the arguments in favour for the shareholder-centric approach outlined above). However, the nature of the creditor-company relationship should not detract focus from the unique role that the company plays in its community, and on those persons within the community who depend on the company to fulfil its needs. Therefore, it is the role of the company itself that requires regulation rather than the nature of the relationship between the role-players themselves.[137] Finally, other criticisms of the stakeholder approach includes the lack of an enforceable remedy for stakeholders in the event that directors fail in their duties towards stakeholders,[138] and that the courts would become increasingly involved in the business decisions of directors.[139]

(iv) The enlightened shareholder-value approach

The above criticisms raise important considerations in answering the question in whose interest the company should act. Mongalo explains what is at the core of the enlightened shareholder-value approach where he, notes the value of the shareholders in the company and the importance of prioritising the shareholders in a profit company. However, he goes further to say that '…it defeats the logic that almost all benefit corporation statutes continue to empower *only shareholders* [particularly in a public company setting]'[140] (my emphasis).[141] Ultimately, the enlightened shareholder-value approach takes into account the 'legitimate interests and expectations'[142] of stakeholders as a whole (that is, constituencies beyond the shareholders) where these also coincide with the interests of shareholders and thus contributes to shareholder value.[143] In other words, broader interests must, as a whole, be considered as subordinate to the interests of shareholders, who remain the primary constituency of a company, such that the objective of profit maximisation remains a the main priority of a company as opposed to defeating this objective entirely by, for example, accounting to each and every stakeholder.[144] In this respect, it is important to bear in mind the 'too many masters'[145] argument when including stakeholder concerns whilst still needing to address shareholder

[136] Ibid at 59.

[137] Ibid.

[138] Ibid at 59-60. However, s165 loc cit note 2 could potentially serve as a remedy in this regard.

[139] Ibid. See also *Re Smith's* case supra note 67 at 306.

[140] Tshepo H. Mongalo *Corporate Actions and the Empowerment of Non-Shareholder Constituencies* (unpublished PhD thesis, University of Cape Town, 2015) 234.

[141] Tshepo Mongalo 'Supervision of The Use of Corporate Power as The Ultimate Purpose of Directorial Duties and The Advisability of Corporate Law Enforcement in the Public Interest' (2017) 1 *JCCL&P* 17 at 19.

[142] Jonathan Rushworth 'Relational Companies: Towards Responsible Capitalism' (2017) 1 *JCCL&P* 49 at 64.

[143] Ibid.

[144] Cassim et al op cit note 3 at 519.

[145] Irene-Marie Esser 'The Enlightened Shareholder-Value Approach Versus Plurism in the Management of Companies' (2005) *Obiter* 719 at 720.

concerns as a matter of priority –

> '…all the various stakeholder groups would have to be identified and the nature and the extent of the directors' responsibilities to them determined. The result would be that the directors would not effectively be accountable to anyone since there would be no clear yardstick for judging their actions.'[146]

Surely, the objective of corporate governance as a whole is to enhance accountability rather than to reduce or diminish it. Therefore, directors must apply their minds, with the necessary care, skill and diligence that is required of directors generally under section 76(3)*(c)* of the 2008 Act, when including stakeholder interests as part of their decision-making processes. Ultimately, the enlightened shareholder-value approach accounts for the modern company in that the company stands to benefit from an enhanced retention of employees, suppliers and customers, as well as an improved image and reputation of the company within its local community.[147] It is argued that it simply makes good business sense for companies to practise good corporate governance and corporate social responsibility.[148] This accords with the notion that the interests of stakeholders are a 'means to an end, but not an end in itself'.[149]

It must be asked which view South African company law subscribes to. Early case law, such as the *Parke* case,[150] shows that courts applied the shareholder-centric approach under the common law.[151] In this case, it was held that directors owed their fiduciary duties towards the company (that being the collective body of shareholders in the short-term and long-term) such that directors could not act in the interests of their employees because employees were not in the short-term nor long-term interests of the company when it was being wound up.[152] However, Davis and Le Roux show that this position has since changed in that directors can ensure 'sustainable returns'[153] for the company, whilst also allowing the employees of the company to participate, and have access to certain information in the company, or hold directors accountable for their actions or lack thereof.[154] For example, the 2008 Act provides employees with a derivative action, and participation rights when it

[146] Ibid. See also Giles Proctor & Lilian Miles 'Duty, Accountability and the Company Law Review' (1999) *Company Lawyer* 1.

[147] Cassim et al op cit note 3 at 519.

[148] Ibid.

[149] Jennings op cit note 87 at 60.

[150] *Parke v Daily News Ltd* 1962 2 All ER 929 (ChD).

[151] Ibid.

[152] Ibid.

[153] Dennis Davis & Michelle Le Roux 'Changing the role of the corporation: A journey away from adversarialism' (2012) *Acta Juridica* 306 at 323-24.

[154] Ibid.

comes to business rescue proceedings.[155] The business rescue provisions in the 2008 Act are rather innovative and stakeholder inclusive.[156] This is evident from the definition of an 'affected person' in the 2008 Act which expressly includes employees;[157] the direct recognition and protection of the fair and equitable interests of employees;[158] and the right of employees be notified of the adoption or rejection of the business rescue plan.[159]

Nevertheless, shareholder-centrism remains the dominant approach in South African company law tempered by an enlightened shareholder-value approach. This is clear from what is meant by 'the best interests of the company' in section 76(3)*(b)* of the 2008 Act as discussed in detail below.[160] However, there is arguably scope for consideration of broader stakeholder interests in the 2008 Act when these interests are in alignment with the best interests of the company (the enlightened shareholder-value approach). For example, where the 2008 Act requires the inclusion of a social and ethics committee in a public company, as discussed below.[161] Thus the 2008 Act presents a conundrum: on the one hand supporting shareholder centrism, on the other a clear move towards a more enlightened perspective.[162] The latter perspective is supported by Esser who argues that stakeholders are protected under the 2008 Act and she draws on the King III report (which is discussed below) in this respect.[163] It is, therefore, necessary to take a closer look at corporate governance in the 2008 Act by focusing on the fiduciary duty to act in the best interests of the company, and the King Reports respectively.

V THE FIDUCIARY DUTY TO ACT IN THE BEST INTERESTS OF THE COMPANY

Under the common law and the 2008 Act, directors owe fiduciary duties to the company.[164] These duties create a certain level of conduct to be as expected from directors on the basis that section 66(1) of the 2008 Act, which vests the powers, functions, and management of the business and affairs of the company in the board of directors. Both the common law and provisions under the 2008 Act

[155] Ibid. See also s165(2)(c) loc cit note 2 in which employees (their representatives or registered trade union) have legal standing to serve a demand on the company where the legal interests of the company have been compromised.

[156] Cassim et al op cit note 3 at 868. See also s7(k) loc cit note 2.

[157] Ibid s128(1)*(a)(ii)* and *(iii)* which defines an 'affected person' in a business rescue proceeding as a registered trade union representing employees, and employee's representatives.

[158] Ibid s136 which protects the jobs of employees, or subjects their retrenchments to the respective labour laws.

[159] Cassim et al op cit note 3 at 899.

[160] Michelle Havenga 'Director's fiduciary duties under our future company law' (1997) 9 *SA Merc LJ* 310 at 316.

[161] See section V below.

[162] Jennings op cit note 87 at 60. See also section V below.

[163] Irene-Marie Esser 'Corporate Social Responsibility: A Company Law Perspective' (2011) 23 *SA Merc LJ* 317 at 324.

[164] Cassim et al op cit note 3 at 509. See also s1 loc cit note 2 which defines a director as 'a member of the board of a company, as contemplated in s66, or an alternate director and includes any person occupying the position of director or alternate director, by whatever name designated'.

(which itself has partially codified the common law) govern fiduciary duties and apply in a parallel manner.[165] While fiduciary duties are essentially founded on '…loyalty, good faith and avoidance of conflicts of interest and duty',[166] it is worth examining the elements of what is meant by a 'fiduciary'. A fiduciary is characterised as having a discretion of power coupled with the ability to unilaterally exercise this power such that it would affect the beneficiary's legal or other interests.[167] Therefore, the beneficiary is essentially vulnerable or, in extreme terms, at the mercy of the fiduciary owing to the inherently unequal balance of power in this relationship.[168] These elements shed light as to why duties exist under common law and statutory law – when entering into a relationship with a fiduciary, the beneficiary always bears the potential risk of abuse of power by the fiduciary, thus '[t]he [fiduciary] duties are meant to be prophylactic and preventative'.[169]

The fiduciary duty in section 76(3)*(b)* of the 2008 Act is of particular relevance to this research report as it expressly provides that a director, when exercising the powers and functions of a director, *must* do so 'in the best interests of the company' (my emphasis).[170] It must be asked what is meant by 'the best interests of the company'. It is certainly not a simple and easy task to define the concept 'best interests' as 'the concept remains so miserably indeterminate'[171] and undefined in the 2008 Act.[172] The traditional view is that the best interests of the company means that directors owe their duties exclusively to the company's shareholders since it has already been established under common law that 'the company' refers to the '…interests of the collective body of present and future shareholders'.[173] Perhaps this implies that the drafters of the 2008 Act had intended for section 76(3)*(b)* to be reflective of the traditional shareholder-centric approach.[174]

However, other academics, such as Mongalo, have argued against the traditional view. Mongalo argues that the common law rules on directors' duties have resulted in two incorrect conclusions – first, that duties are owed exclusively to shareholders, and secondly, that shareholders are the only constituency in the company to be accounted for.[175] Consequently, Mongalo recognises

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165 Ibid at 507; 523.

166 Ibid at 509.

167 Ibid at 507.

168 Ibid at 513.

169 Ibid at 523.

170 See also s76(3)*(a)* loc cit note 2 which provides that directors must exercise their powers and functions 'in good faith and for a proper purpose'.

171 Esser *Stakeholder Debate* op cit note 98 at 357. See also R. Parsons 'The Director's Duty of Good Faith' (1967) 5 *Melbourne University LR* 395 at 396 and Gwanyanya op cit note 69 at 3109.

172 Ibid.

173 Ibid. See also Cassim et al op cit note 3 at 515.

174 Ibid.

175 Mongalo *Supervision* op cit note 141 at 26.

the modernity of the company and its socio-economic context in that

> '[t]he unquestioned connection between the corporate legal enforcement framework and the conventional role of directorial duties is out of date and needs to change to reflect the reality of modern business…*directorial duties clearly concern the supervision of the use of corporate powers for the overarching purpose of minimising or eradicating directorial self-serving conduct, and, thus, cannot possibly be owed exclusively to shareholders* (my emphasis).'[176]

Moreover, Mongalo argues that the real role of directors' duties, *especially in a public company setting* (given the high degree of scandal and inefficiency in modern public companies), is to prohibit or restrain directorial corruption or self-dealing in order to better enhance the interests of the shareholders *as well as all other corporate constituencies* whose financial well-being is linked to the sound running of and ultimate success of the company (my emphasis).[177] It is based on the logic that the twenty-first century company has various groups of people to consider beyond just the shareholders, that Mongalo notes the 'dysfunctional'[178] and unsustainable notion of shareholders being the one and only focus of directors.[179] While this might appear as an extreme assertion to the traditional company lawyer, it is submitted that it is an assertion with which I must agree because of how high the stakes are for the modern company. For instance, the modern company must ensure profit-making (which in itself can be daunting in a volatile economic climate); investor protection; building steady company-creditor relations; protecting its reputation; and contributing to the economy and the surrounding community where appropriate.[180] This view is reiterated by Esser where she considers that public opinion had shifted towards the recognition of a broader set of interests, beyond the shareholders, which includes, amongst others, the investors of a company, their employees, consumers who contribute towards the profits of the company, the general public and the environment.[181]

I argue that the 2008 Act embodies Mongalo's line of thinking to a certain degree particularly in respect of public companies. For example, section 72(4) of the 2008 Act provides for the appointment of a social and ethics committee, as prescribed by the Minister, if it is in the public interest to do so having regard to the company's annual turnover; workforce size; and the nature and extent of the activities of the company.[182] Thus, every listed, state-owned, and certain private

[176] Ibid at 20; 25.
[177] Ibid at 26.
[178] Ibid.
[179] Ibid.
[180] See *Stilfontein's* case supra note 8 para 16.7.
[181] Esser *CSR* op cit note 163 at 350.
[182] Section 72(4)*(a)* loc cit note 2.

companies (where it is in the public interest to do so) must have a social and ethics committee.[183] The main function of a social and ethics committee is to monitor the company's activities so as to promote good corporate citizenship.[184] Cassim notes the following good corporate citizenship goals to be achieved by means of a social and ethics committee –

> '…the company's promotion of equality and the prevention of unfair discrimination; contribution to the development of the communities in which the company's activities are predominantly located; its record of sponsorship, donations and charitable giving; the environment, health and public safety; consumer relationships; and labour and employment.'[185]

Evidently, a social and ethics committee incorporates the interests of various stakeholders. This makes practical sense given the potential positive or negative impact by such companies on the public. Cassim argues that the social and ethics committee constitutes a legal adoption of the enlightened shareholder-value approach and of corporate social responsibility.[186] However, it falls short of a set of fiduciary duties given that the fulfilment of these functions can easily translate into 'mere box-ticking'[187] by directors, as opposed to it being an altruistic and concerted effort towards corporate social responsibility.[188] Moreover, the absence of fiduciary duties, or other legal duties in general, towards stakeholders means that stakeholders have no real enforcement mechanisms, unless they have the legal standing to protect the company's legal interests under section 165 of the 2008 Act (the derivative action provision).[189] At most, a company's failure to create a social and ethics committee would result in receiving a compliance notice.[190] While this appears to be a rather light penalty, it is argued that this is 'not to be trifled with',[191] thus implying that it is not as minor as it may seem.[192]

A further concern with the social and ethics committee is that there are no statutory guidelines in the 2008 Act, or elsewhere, to aid the committee in ranking the interests of stakeholders against

[183] Cassim et al op cit note 3 at 522.

[184] Ibid.

[185] Ibid at 522-23.

[186] Ibid at 523.

[187] Ibid.

[188] Ibid.

[189] Ibid. See also s165(2)*(a)-(d)* loc cit note 2 which provides for a shareholder, director or prescribed officer, a registered trade union or other representative of employees of the company, or a person who has been granted leave by the court to provide the company with a demand to begin or continue legal proceedings 'to protect the legal interests of the company'. This route may prove challenging for stakeholders as their interests would need to coincide with the legal interests of the company.

[190] Cassim et al op cit note 3 at 523.

[191] Ibid.

[192] Ibid.

those of the shareholders.[193] There seems to be a discretion left to the committee in this regard. For example, a conscientious mining company is likely to place a higher ranking on environmental concerns than it would place on its consumer relationships.[194] Jennings argues that stakeholder interests must be established and prioritised on a case-by-case basis – a point which I reiterate further below.[195]

It is, however, interesting to note that the Companies Amendment Bill[196] (herein after referred to as 'the Bill') will amend section 61 of the 2008 Act to include the presentation of a social and ethics committee report at a shareholders meeting in a public company.[197] The inclusion of this report arguably adds authority to the social and ethics committee of the 2008 Act as it is now mandatory to present the director's report alongside the annual financial statements; audit committee report; and remuneration report.[198] Moreover, the Bill includes an amendment of section 72 of the 2008 Act, which especially deals with the formation of a social and ethics committee [as opposed to the more general provision on board committees contained in section 72(3)].[199] This implies an intention by the legislature for public companies to take the social and ethics committee more seriously in practice.

However, the amended section 61 implicitly maintains that directors still owe their duties to shareholders. Ultimately, the social and ethics committee need only bring the attention of the board of directors to a matter, but the board still reports to the shareholders and is accountable as such.[200] This generally enhances the traditional shareholder-centric approach since shareholder interests would naturally trump stakeholder interests in meetings, and directors are not obliged in any way to fulfil stakeholder interests.[201] Jennings seems to be correct in stating that the predominant approach followed in the 2008 Act is the shareholder-centric approach.[202]

Therefore, the position in the King IV Report on what is meant by the 'best interests of the company' must be compared with the position in the 2008 Act.[203] While it is traditionally meant that directors owe their duties to the company and its shareholders alone, it must be noted that the company comprises of numerous interests, including that of both shareholders and other stakeholders

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[193] Jennings op cit note 87 at 62.

[194] Ibid.

[195] Ibid. See also section VIII below.

[196] No. 969 of 2018.

[197] Ibid.

[198] Ibid. Section 61(8)*(a)* loc cit note 2.

[199] Ibid.

[200] Jennings op cit note 87 at 62.

[201] Ibid at 62-3

[202] Ibid at 63.

[203] Institute of Directors in Southern Africa (IODSA) 'King IV: Report on Corporate Governance for South Africa 2016' available at *http://www.iodsa.co.za,* accessed on 10 June 2018.

(employees, consumers, the community and the environment).[204] Consequently, this would require directors, acting in good faith, to first and foremost act in the best interest of the company as a separate legal entity, but thereafter to recognise and to blend these interests (the recommendations of which are discussed in more detail below).[205] This approach better accommodates for the modern company law climate, hence the King Reports will be analysed in more detail below.

VI CORPORATE GOVERNANCE AND THE KING CODE

It is necessary to outline the positions held in the King Reports in chronological order so as to showcase the evolution of corporate governance culture. The first King document (King I) was released in 1994 and it provided corporate governance guidelines.[206] In 2002, King I was replaced by King II.[207] A crucial feature of King II was the 'move from a single to the triple bottom line',[208] which tied the economic, social, and environmental spheres together as they relate to a company.[209] However, it must be noted that this did not amount to altering the prime purpose of the company, that being profit-making and directors' accountability to their shareholders.[210] Instead, directors have been urged to approach stakeholder relationships cautiously by, at a minimum, considering these interests when it is appropriate to do so.[211] It would be an extremely onerous expectation to hold directors accountable to each and every stakeholder as this would have the reverse and undesirable effect of directors being accountable to no one.[212] This is counter the very essence of corporate governance as found in the King Reports.

In 2010, the King III came into effect.[213] King III further promoted the triple bottom line approach as it encouraged boards of directors to consider *the legitimate interests and expectations of stakeholders* other than those of the shareholders (my emphasis).[214] However, King III did not provide any direction as to whether the enlightened shareholder-value approach or the stakeholder approach was to be followed in this respect.[215] Nevertheless, King III placed a 'real emphasis'[216] on company

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204 Ibid. See also Esser et al *Stakeholder Debate* op cit note 98 at 346-60.
205 Ibid. See also section VII below.
206 Esser *ESVA* op cit note 145 at 722.
207 Ibid.
208 Ibid.
209 Ibid.
210 Ibid.
211 Tshepo Mongalo 'The Emergence of Corporate Governance as a Fundamental Research Topic in South Africa' (2003) *SALJ* 173 at 177.
212 Ibid.
213 Kathy Coleman 'The King is dead; long live the King' (2009) *Without Prejudice* 8 at 8.
214 Jennings op cit note 87 at 61.
215 Ibid.
216 Coleman op cit note 213 at 9.

ethics and the notion of being a good ‘corporate citizen’.[217] Corporate citizenship has been defined in the King III Report as recognising that the company, as a juristic person with legal standing, rights, obligations and responsibilities, forms an integral part of and is legitimated by its broader society.[218] However, King III maintained that directors must act in the best interests of the company and its shareholders as per the common law.[219]

In 2016, the Institute of Directors in Southern Africa (IODSA) noted that ‘[t]he twenty-first century has been characterised by fundamental changes in both business and society’.[220] Such changes can be found in the rise of civil society activism against various company practices; the increased conscientiousness of investors and young businessmen; and the occurrence of greater expectations from stakeholders now more than ever before.[221] Hence, King IV was put into effect.[222]

King IV defines ‘corporate governance’ in light of four main factors, namely ethical culture; good performance; effective control; and legitimacy.[223] Interestingly, ‘ethical culture’ is listed first. Ethical culture expects directors to anticipate and prevent the detrimental consequences of the company’s activities on the economy, society and environment in which it operates.[224] This signifies the extent to which the drafters of King IV expect directors to exercise corporate governance. Indeed, the standard herein is a high one.

Furthermore, King IV accounts for the fact that the South African economy is capitalist in nature, thus IODSA suggests an ‘inclusive capitalism’[225] rather than a ‘financial capitalism’.[226] Inclusive capitalism would allow for a developing country, such as South Africa, to more closely embody a sense of ‘integrated thinking’[227] –

> ‘The more an organisation’s business model positively impacts on society and the environment, the more the quality of life in developing economies will improve. This improvement, in turn, will positively affect the prospects for those organisations.’[228]

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[217] Ibid.

[218] Institute of Directors in Southern Africa (IODSA) ‘King IV: Report on Corporate Governance for South Africa 2016’ available at *http://www.iodsa.co.za,* accessed on 10 June 2018.

[219] Institute of Directors in Southern Africa (IODSA) ‘King III: Report on Corporate Governance in South Africa 2009’ available at *http://www.iodsa.co.za*, accessed on 30 March 2018.

[220] Institute of Directors in Southern Africa (IODSA) ‘King IV: Report on Corporate Governance for South Africa 2016’ available at *http://www.iodsa.co.za,* accessed on 10 June 2018.

[221] Ibid.

[222] Ibid.

[223] Ibid.

[224] Ibid.

[225] Ibid.

[226] Ibid.

[227] Ibid.

[228] Ibid.

This point must be emphasised for two main reasons – first, this is yet another source arguing that the company's consideration of stakeholder interests is in fact sustainable for the company, and secondly, this approach complements a capitalist economy and society rather than operating against it. It is argued that the latter would prove extremely counter-productive for companies, corporate governance and the economy as a whole. This research report does not propose to reduce the importance of the motive for a company to make a profit, but instead argues for an inclusive approach to broader stakeholder interests without delegitimising the interests of shareholders (that is, an enlightened shareholder-value approach). This approach seems to be an ideal way in which directors can achieve a more profitable yet productive and sustainable company in its community.

It is then understandable why, in the King IV Report, IODSA refers to 'stakeholder management'[229] by emphasising that '…management needs an ongoing relationship with stakeholders'.[230] This would also facilitate the identification of reasonable and legitimate stakeholder interests, and it would prevent the unreasonable expectation of directors having to account for each and every stakeholder concern.[231] It remains unclear what is meant by 'reasonable and legitimate' stakeholder interests, but it can be reasonably inferred that these interests would need to be in alignment with the best interests of the company (the ultimate standard). Consequently, stakeholder interests would have to be judged on a case-by-case basis – it can hardly be contended that a one-size-fits-all approach can be used to establish relevant stakeholder interests.[232] Some companies have appointed a 'corporate stakeholder relationship officer',[233] who bears the role of identifying and consolidating legitimate stakeholder interests, as a means to this end.[234]

Ideally, King IV proposes a stakeholder-inclusive approach as it identifies the relationship of dependency between the company and the stakeholder (and vice versa), and that a balancing exercise is required when trading off general stakeholder interests against shareholder interests who are the main stakeholders of the company.[235] The approach operates in stark contrast with the shareholder-centric approach outlined above –

> 'Adopting the stakeholder-inclusive approach means that *the best interests of the company are not necessarily always equated to the best interests of shareholders*…shareholders do not

[229] Ibid.

[230] Ibid.

[231] Ibid.

[232] Justine Krige & Gasant Orrie 'Large private companies and King IV – proportionality is the answer' (2018) *Without Prejudice* 13 at 13.

[233] Institute of Directors in Southern Africa (IODSA) 'King IV: Report on Corporate Governance for South Africa 2016' available at *http://www.iodsa.co.za,* accessed on 10 June 2018.

[234] Ibid.

[235] Ibid.

> necessarily have a predetermined precedence over other stakeholders…Stakeholder inclusivity means that the board considers other stakeholders not merely as instruments to serve the interests of shareholders, but as having intrinsic value for decision-making in the best interests of the company over time…*The interests of shareholders and stakeholders are interdependent; thus, following [this approach] maximises this symbiosis to promote the company's long-term sustainability* (my emphasis).'[236]

As compared to its predecessors, King IV provides for a more extensive definition of corporate governance and it provides greater recognition to the various stakeholders of a company. It is, however, important to bear in mind that the King Reports are voluntary in nature – that is, the reports do not constitute binding and enforceable law.[237] However, the King Reports should not be viewed as 'legally irrelevant'[238] because of its lack of enforceability since they are persuasive as the courts have incorporated the reports in their legal analyses. [239] The effect of such judicial inclusion has served two main purposes: first, it lends an understanding on how to contexualise and apply stakeholder inclusivity, but, as Esser argues, it has also made the King Reports stronger than mere recommendations as the reports are instrumental for directors in complying with their duties under the 2008 Act.[240] Hence, in the *Stilfontein* case, the King Reports helped the court reach a conclusion that the directors were in breach of their duties.[241] This point must be emphasised as directors bear a risk where they do not comply with their duties under the 2008 Act, that is the incurrence of liability, which is quite extensive in section 77 of the 2008 Act. The *Stilfontein* case is also a clear example of how the court applied the King Code standards where mismanagement of water directives by a public company could have negatively impacted the lives of miners and the environment (by way of health risks, pollution, and flooding) –

> 'A well-managed company will be aware of, and respond to, social issues, placing a high priority on ethical standards. A good corporate citizen is increasingly seen as one that is non-discriminatory, non-exploitative, and responsible with regard to environmental and human rights issues. A company is likely to experience indirect economic benefits, such as improved productivity and corporate reputation, by taking those factors into consideration.'[242]

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[236] Ibid.

[237] Cassim et al op cit note 3 at 521. See also P. Armstrong 'The King Report on Corporate Governance' (1995) *Juta Business Law Journal* 65; Derek Botha 'Confusion in the King Report' (1996) *South African Mercantile Law Journal* 26; Gwanyanya op cit note 68 at 3110.

[238] Ibid.

[239] Ibid.

[240] Esser *CSR* op cit note 163 at 328.

[241] Ibid at 330.

[242] *Stilfontein's* case supra note 8 para 16.9. See also Lise Smit 'Human rights litigation against companies in South African courts: A response to *Manyaki v Anglogold Ashanti* 2011 (3) SA 237 (CC)' (2011) *SAJHR* 354 at 361-62.

The legal framework created by the 2008 Act and the King Reports is that there exists both elements of the enlightened shareholder-value approach, which prioritises the shareholder while creating room for other stakeholder considerations where it is in the best interests of the company, and elements of stakeholder inclusivity, but Esser has argued that it is unclear which approach is preferred.[243] Hence, Esser further contends that directors ought to balance the various interests of stakeholders,[244] which naturally includes shareholders. An inclusive approach is, however, possible upon interpretation of the 2008 Act where sections 7 and 5(1) are quite compatible with King IV, which in turn informs the best interests of the company and the reasonable expectations stakeholders may have of directors, especially considering that section 7*(d)*, in particular, does not confer direct rights on stakeholders.[245] Directors are then better able to balance the various interests they need to consider on a daily basis to ensure the optimum functioning of the company. This is discussed in detail below.

VII TOWARDS A BALANCED APPROACH

Regard must always be had to the context in which the company operates especially when applying legislation such as the 2008 Act. Mongalo correctly recognises that shareholder-centrism in itself is outdated, and that profit – while the pivotal purpose – cannot be the only purpose of a company.[246] On the other hand, the stakeholder approach is far too drastic a shift especially in a capitalist context, such as that of South Africa's economy and society.[247] Thus, the enlightened shareholder-value approach appears to be an achievable balance – it continues to prioritise shareholders and profit whilst widening the framework for the consideration of stakeholder interests where it is in the best interests of the company to do so. However, there remains practical difficulties around stakeholder inclusivity which may only be ironed out as the 2008 Act and the South African economy and society matures. The bottom line is that companies need to be profitable, and directors need to be accountable to the company and its shareholders. Furthermore, as argued by Jennings, one of the main obstacles to corporate governance, and the notion that the company has a role to play in the socio-economic sphere, is that the 2008 Act itself requires a predictable environment and this this must be taken into account when balancing the various interests a company must consider.[248]

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243 Esser *CSR* op cit note 163 at 334.

244 Ibid.

245 Ibid at 324.

246 Tshepo Mongalo 'South Africanizing company law for a modern competitive global economy' (2004) 121 *SALJ* 93 at 114.

247 Institute of Directors in Southern Africa (IODSA) 'King IV: Report on Corporate Governance for South Africa 2016' available at *http://www.iodsa.co.za*, accessed on 10 June 2018.

248 Jennings op cit note 87 at 76.

I propose that the underpinnings of the enlightened shareholder-value approach coupled with the purposes of the 2008 Act, its interpretation provision, and the recommendations put forward in the King IV Report (particularly those on stakeholder inclusivity) can be used in an eclectic manner so as to fill any gaps or deficiencies in each. In other words, there must be a blend of interests as outlined above, which in the words of Sachs, is perhaps better articulated as the need to *harmonise* private-sector incentives and socio-economic considerations (my emphasis).[249] To further explain what a blending of interest would entail, Esser's view is that there ought to be an *interaction* between business and the community (my emphasis).[250] Esser further argues that, in her view, such interaction is already in existence in a South African context where the 2008 Act and the King Reports are examples of involvement from the state and society.[251] It is argued that such interaction should be more deliberately emphasised in practice by the directors of a company, and by the courts (with due regard to the fact that the court in the *Stilfontein* case has quite deliberately highlighted this interaction, as outlined above). Furthermore, Esser's emphasis on an interaction between the 2008 Act and the King Reports could sustain an argument that the enlightened shareholder-value approach and stakeholder inclusivity are not mutually exclusive approaches, but that there is an overlap between these approaches to the extent that inclusivity is in the best interests of the company.

Moreover, international trends can also serve as a useful guide in certain respects. For example, in 2010, Professor John Ruggie held consultations with civil society stakeholders, ranging from those belonging to Amnesty International to those belonging to the Organisation for Economic Co-operation and Development (OECD) watch, as a means to establish the human rights violations committed by transnational corporations.[252] Perhaps this could serve as a model for domestic companies to draw on – to have a consultation process in which relevant stakeholders can engage in dialogue with companies.[253] It must be made clear that the primary purpose of these consultations would be to enable directors to better identify reasonable and legitimate stakeholder interests in accordance with the best interests of the company.

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[249] Jeffrey Sachs *The End of Poverty and Common Wealth: Economics for a Crowded Planet* (2008) 1.

[250] Esser *CSR* op cit note 163 at 334.

[251] Ibid.

[252] The United Nations "Consultations with civil society stakeholders on the implementation of the UN 'Protect, Respect, and Remedy' Framework: Summary Note" available at *https://www.business-humanrights.org/sites/default/files/media/documents/report-from-ruggie-civil-society-consultation-geneva-11-12-oct-2010.pdf*, accessed on 26 August 2018. See also John Ruggie 'Report of the Special Representative of the Secretary-General on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises' (2011) 29(2) *Netherlands Quarterly of Human Rights* 224 at 226.

[253] See also The JSE 'JSE Regulatory Review Consultation Paper issued for public comment' available at *https://www.jse.co.za/articles/Pages/JSE-Regulatory-Review-Consultation-Paper-issued-for-public-comment.aspx*, accessed on 28 November 2018 in which the JSE held such process with the public following the alarming number of corporate scandals in public listed companies, such as Steinhoff.

Companies, large and small, have a certain degree of power over the societies in which they exist.[254] Naturally, larger companies would have more power and impact thansmaller companies , but it does not change the fact that, regardless of the size of the company, there is a stronger need to incorporate stakeholder interests, hence the need for the board of directors and the shareholders of a particular company to exercise good corporate governance. The board of directors would need to exercise 'effective leadership based on ethical foundation'[255] in that

> '[i]t is responsible for the strategic direction and the control of the company…The board of directors should strive to achieve the appropriate balance between its various stakeholder groupings, and is urged to take into account, as far as possible, the legitimate interests and expectations of its stakeholders when making decisions in the best interests of the company'.[256]

While this research report is not focused on shareholder activism, it is argued that shareholder activism must be encouraged over shareholder apathy where 'passive'[257] shareholders tend to 'undermin[e] good levels of compliance by management'.[258] This is especially the case in the South African public company law arena (but should also be applied in the private company law arena) where 'corporate governance…has been characterised by one major scandal or other over the last ten years'[259] with negative effects on the reputation, employees, and consumer relationships of such companies.[260] This cannot be said to be in the best interests of the company. An example of poor corporate governance having resulted in a detrimental effect on reputation can be seen from KPMG, a leading auditing firm. KPMG's reputation was tarnished by its associations with state capture and high-level corruption in South Africa (including the recent VBS bank scandal).[261] The impact of reputational damage as a result of poor corporate governance should not be underestimated. The company's negative image can cause a loss of clientele, which, in turn, results in a loss of profit. This is aside from the incurrence of company costs (for example, the legal and public relations fees that come with damage-control and handling public scandals). It is ultimately argued that companies ought to 'advance corporate governance'[262] by means of the enlightened shareholder-value approach,

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[254] Esser *CSR* op cit note 163 at 317.
[255] Cassim et al op cit note 3 at 470. See also *Mpofu's* case supra note 7 para 60.
[256] Ibid.
[257] Ibid at 497.
[258] Ibid.
[259] Vishnu Padayachee 'King IV is here: Corporate Governance in South Africa Revisited' (2017) 66 *New Agenda* 17 at 19.
[260] Ibid.
[261] The Mail & Guardian 'KPMG woes deepen after VBS bank scandal' available at *https://mg.co.za/article/2018-04-15-kpmg-woes-deepen-after-vbs-bank-scandal*, accessed on 28 November 2018.
[262] John Plender 'Shareholders are being dethroned as rulers of value' available at *https://www.ft.com/content/42871952-0463-11e9-99df-6183d3002ee1*, accessed on 2 January 2019.

which continues to prioritise the shareholder, as this is currently 'the best hope'[263] towards a workable stakeholder inclusivity.[264]

VIII CONCLUSION

There was undoubtedly a need for company law reform via the enactment of the 2008 Act. The 2008 Act provides for a far more flexible, simple and efficient means for a company to be incorporated and to function in a modern setting. A distinctive feature of the modern company includes the integration of various stakeholder interests, such as employees and the environment.[265] Thus, it has been argued that directors in a modern company must blend and better incorporate such interests, as opposed to viewing shareholder interests as the be all and end all. That is not to say that shareholder interests and profit maximisation are not to be prioritised – they must indeed continue to be of utmost priority for the health and well-being of the company in the South African economy. However, directors ought to consider the prospect that the best interests of the company can be furthered by including stakeholder interests within appropriate and reasonable boundaries. This can be achieved by relying on practical guidelines, for example, the nature of the company's business; the nature of the stakeholder; and the priority of the stakeholder's concern or interest. This is certainly not an easy task for directors as stakeholder interests need to be balanced carefully and strategically against shareholder interests and the need to make a profit.

Under the 2008 Act, the purposes in section 7 are clear and inclusive of stakeholder interests, but it is broadly defined and thus of little assistance to the courts in its interpretation. The same can be said for 'the best interests of the company' standard in the 2008 Act – it is undefined and directors have a significant degree of discretion in this regard. However, the common law does scaffold this standard by restricting it to the collective body of shareholders, thus emphasising a shareholder-centric approach under the 2008 Act. Yet the 2008 Act also embodies an enlightened shareholder-value approach towards public companies, for example, in that it prescribes a mandatory social and ethics committee.

The King Reports, especially King IV, strongly emphasise stakeholder inclusivity, but this is often sidelined because of its soft and non-binding nature. On this note, it is important to guard against rendering the reports as irrelevant, but rather to use the following in a more interactive manner – section 7 of the 2008 Act; the best interests of the company standard; the King reports; the nature of the relevant company and its stakeholders; and the socio-economic context of South Africa so as to

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[263] Ibid.

[264] Ibid.

[265] Cassim et al op cit note 3 at 517.

identify the potential impact the company's consideration of stakeholder interests may have in this respect.[266]

Ultimately, the 2008 Act provides for purposive provisions (such as section 7) as well as provisions that contain clear and specific guidelines, which moves towards an enlightened shareholder-value approach when read together. This should be emphasised deliberately by directors, practitioners and courts. While progress has been made under the 2008 Act, not enough has been made in a rapidly changing modern and capitalist context to more strongly include stakeholder interests. A healthy balance must be struck between the different sources of law to shape a more stakeholder-inclusive, but profit-driven approach and, hence, a thriving and sustainable South African economy.

[266] Ibid at 504.