

**BG** Bowman Gilfillan

---

**DIRECTORS AND  
OFFICERS LIABILITY  
INSURANCE**



You think  
ventures.  
We think  
vulnerability  
cover.



*Our horizons are as broad as your business vision.*



## *The Bowman Gilfillan Africa Group*

Bowman Gilfillan Africa Group is one of Africa's premier corporate law firms, employing over 400 specialised lawyers. The Group provides domestic and cross-border legal services to the highest international standards across Africa, through its offices in South Africa, Botswana, Kenya, Madagascar, Tanzania and Uganda.

Differences in law, regulation and business culture can significantly increase the risk and complexity of doing business in Africa. Our aim is to assist our clients in achieving their objectives as smoothly and efficiently as possible while minimising the legal and regulatory risks.

While reliable technical legal advice is always very important, the ability to deliver that advice in a coherent, relevant way combined with transaction management, structuring, negotiating and drafting skills is essential to the supply of high quality legal services.

The Group has offices in Antananarivo, Cape Town, Dar es Salaam, Gaborone, Johannesburg, Kampala and Nairobi. Our office in Madagascar, has francophone African coverage in Benin, Burkina Faso, Burundi, Cameroon, Central African Republic, Chad, Congo Republic, Gabon, Guinea, Ivory Coast, Mali, Niger, Rwanda, Senegal and Togo.

We have a best friends relationship with leading law firm Udo Udoma & Bela-Osagie, in Nigeria, which has offices in Lagos, Abuja and Port Harcourt. We also have strong relationships and work closely with law firms across the rest of Africa which enables us to provide or source the advice clients require in any African country, whether on a single country or multi-jurisdictional basis.

We act for corporations, financial institutions, state owned enterprises and governments providing clear, relevant and timely legal advice to assist clients achieve their objectives and manage their legal risks.

Geographical and sector specific teams are utilized to provide clients with the highest standards of service. In the cross-border arena the Group has extensive experience in the resources, energy, infrastructure, financial institutions and consumer goods sectors.

Bowman Gilfillan Africa Group's South African, Kenyan and Ugandan offices are representatives of Lex Mundi, a global association with more than 160 independent law firms in all the major centres across the globe. This association gives access to firms which have been identified as the best in each jurisdiction represented.

## The structure of corporations in South Africa

South Africa ('SA') has a new Companies Act, being Act No. 71 of 2008 (the 'Act'), which came into operation on 1 May 2011. The Act is revolutionary in many respects, not least because its predecessor, the Companies Act No. 61 of 1973 (the '1973 Act'), was enacted almost 40 years ago and was subjected to only a few material policy amendments before its repeal. Many of its provisions were archaic.

SA has a relatively simple classification of limited liability entities. In particular, it recognises only one limited liability entity as being capable of having directors, namely a company. Only two forms of limited liability entities are recognised, namely a company and a close corporation ('CC'), the latter being a limited liability vehicle specifically designed to cater for the small business. It is the SA government's stated policy to phase out the CC. This process has already commenced in that, with effect from 1 May 2011, new CCs are forbidden. SA does not recognise the concept of a limited partnership. Unincorporated trusts and partnerships are common.

The Act provides for various categories of companies, the primary division being between profit and non-profit companies. Profit companies, in turn, comprise public and private companies, amongst others. All types of companies must be incorporated or registered in accordance with the Act, which is administered by a regulatory agency called The Companies and Intellectual Property Commission. Every company must also have a constitution, called its Memorandum of Incorporation ('MOI').

## Who are Directors and Officers?

### STANDARD BOARD STRUCTURE

SA's company law is based primarily on English law. SA thus recognises a unitary board structure only; it has never recognised the management of a company's business as being vested in anybody other than its board of directors. The Act does provide for certain compulsory committees in certain instances, namely an audit committee and a social and ethics committee, both of whose members must be directors. It is common practice amongst large companies for the board of directors to delegate many of its duties to committees of the board and individual employees, such as the chief executive officer. Section 66(1) of the Act codifies the powers of the board. It states: '66(1) 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.'

### THE OFFICER STRUCTURE

The only type of 'officer' recognised by the Act is a 'prescribed officer', another new concept. A prescribed officer is a person (other than a director) who, within a company, exercises or regularly participates to a material degree in the exercise of, general executive control over and management of the whole, or a significant portion, of the business and activities of the company. The aforesaid applies irrespective of any particular title given by the company to an office held or the function performed by the person. Prescribed officers are thus generally limited to a company's chief executive officer or the chief executive officer of a division of the company's business which comprises 'a significant portion' of all the company's businesses. 'Regularly participating in the exercise of general executive control' includes being a member of

a company's executive decision—making committee, commonly called its Exco. But participation in Exco is not the sole test; the participation must also be on a regular basis and must be 'material'.

One of the revolutionary aspects of the Act is that, for the first time, SA's companies' legislation contains a partial codification of the common law duties of directors. Prescribed officers are subject to the same codified duties of directors, as well as to numerous others.

#### ARE SENIOR MANAGERS IN THE COUNTRY CALLED DIRECTORS AND OFFICERS?

Senior managers of companies are not called directors because to do so has the potential to expose that individual to the same liabilities as a director vis-à-vis third parties. It is, however, not uncommon for senior managers to be referred to as divisional directors, though the use of phrases such as 'chief financial/marketing/operating officer' and 'general manager' are far more common.

## Duties of the board

#### WHAT ARE THE DUTIES AND OBLIGATIONS OF THE DIRECTORS AND OFFICERS?

##### The Common Law duties

The common law duties of a director are a unique set of obligations which are owed by the directors to the company they serve, and are therefore mainly protective of the company. In carrying out their duties, directors effectively act as agents of the company. They are, however, more than just agents – they are also fiduciaries vis-a-vis the company, which means that they also have a duty to protect the company's interests. These duties are collectively called 'fiduciary duties'.

Set out below are the categories into which the common law duties of directors may be conveniently divided.

### 1. DUTY TO EXERCISE CARE, SKILL AND DILIGENCE

All directors must perform their duties and functions with care and skill. The degree of care and skill that a director must exercise is measured by the care and skill which may reasonably be expected of a person having that particular director's knowledge and skills in the same circumstances (i.e., a subjective test).

It is clear from case law that a director is not required to be an expert in the type of business which the company conducts unless the director is appointed for his specialist knowledge and skills. Directors are not expected to have any knowledge or to exercise skills which they do not possess.

In coming to a decision, a director is entitled to rely on the opinion of an outside expert. The expert must, however, be qualified to give such advice and, upon receipt of the advice, a director must still apply his mind and exercise his own independent judgment, and not blindly follow the advice of the expert. A director is also entitled to rely on his co-directors and employees of the company but, again, such reliance cannot be unquestioning.

Liability of a director for wrongs committed by the company's employees will only arise where the director has failed to take reasonable care in the selection and supervision of the employees. A common sense view must be taken in estimating whether a director, in taking a particular action, has not done so. A director cannot be expected to attend to every minute business detail and is justified in accepting the reports of subordinates on routine matters. Unless it can be shown that a director knew, or should have known of, or had reason to suspect, the commission of a wrongful act committed by an employee and, having the power to prevent it, failed to do so, the director will incur no liability for the employee's wrongful or unlawful act.

A director must also carry out his duties diligently. Diligence carries with it the necessity to devote a reasonable amount of time and attention to the company's affairs. This depends largely upon the number of directors and the nature of their respective duties.

Failure to exercise proper diligence may indicate that a director has acted negligently and, in some cases, may even indicate that a director has acted dishonestly. For example, if a director had reason to suspect an employee of fraud, failure to investigate the matter might amount to connivance in the fraud and, consequently, to dishonesty.

Ignorance of some fact of which a director should have been aware may also render that director liable. The test is one of reasonableness. The duty to exercise care, skill and diligence is not a fiduciary duty. It is derived from the law of delict/tort.

### 2. DUTY TO ACT IN THE BEST INTERESTS OF THE COMPANY

This is generally regarded as the most important of all the fiduciary duties of directors. It dictates that directors owe their duties to the company they serve, and no one else. Until the 1970s, the courts interpreted this duty to mean that directors must act in the best interests of the general body of the company's shareholders, to the exclusion of all the company's other stakeholders. The common law has now widened this duty to include the duty to also consider the interests of the company's other stakeholders.

### 3. DUTY TO ACT WITHIN THEIR POWERS AND FOR A PROPER PURPOSE

The powers granted to directors can only be used for the purposes for which they were granted; directors cannot exercise their powers for an unauthorised or improper purpose. This occurs essentially where directors act beyond their authority or beyond any limitation placed on their authority by the Act, the common law or the MOI. The consequence of a breach of this duty is that the transaction in question is capable of being cancelled by the company, at its election. If the company suffers loss as a result, it may claim from the recalcitrant director all losses it incurred as a result of such breach.

A director must also act honestly. Any fraud or underhand dealing by a director will, in addition to criminal liability, render that director liable to the

company for any loss suffered by the company as a result or for any profit which that director may have made, even if the company could not itself have made the profit.

A director also cannot use for his own purposes, or disclose, confidential information entrusted to that director by virtue of his office.

### 4. DUTY TO EXERCISE INDEPENDENT JUDGMENT

Each director must exercise an independent, unbiased judgment in reaching the decisions he makes for the company. A director cannot be a 'puppet'. In particular, a director who holds office as such only because he was appointed by the majority shareholder or other person cannot allow that shareholder or person to instruct that director to vote or act in any particular manner.

### 5. DUTY TO AVOID CONFLICTS OF INTEREST

A director must not place himself in a position in which that director has, or may have, a personal interest or a duty to another which conflicts, or may conflict, with the interests of the company or with that director's duties to the company. A director cannot prefer his own interests to those of the company.

If the director breaches this duty, the company may recover damages caused by the breach from the director personally.

A director is also required to make full disclosure of the facts relating to any interest that director may have under a contractual arrangement in which both that director and the company are involved.

## 6. THE CORPORATE OPPORTUNITY AND NO-PROFIT RULES

Except with full disclosure to, and the consent of, the remaining directors, a director may not make a profit by using his position as a director to do so.

If a director concludes a transaction or acquires an opportunity for himself which was, in fact, a transaction or an opportunity that was available to the company, then the law will disregard the transaction or opportunity and will treat it as having been entered into or acquired by the company. If it is no longer possible for the company to enter into that transaction or acquire that opportunity, the company may claim from the director any profits the director may have made and/or any damages it may have suffered.

In *Da Silva and Others v CH Chemicals (Pty) Ltd 2008(6) SA 620 (SCA)*, Scott JA described the corporate opportunity and the no profit rules as follows:

‘It is a well-established rule of company law that directors... may not make a secret profit or otherwise place themselves in a position where their fiduciary duties conflict with their personal interests (*Robinson v Randfontein Estates Gold Mining Co Ltd 1921 AD 168 at 177*).

A consequence of the rule is that a director is in certain circumstances obliged to acquire an economic opportunity for the company, if it is acquired at all. Such an opportunity is said to be a ‘corporate opportunity’ or one which is the ‘property’ of the company. If it is acquired by the director, not for the company but for himself, the law will refuse to give effect to the director’s intention and will treat the acquisition as having been made for the company. The opportunity may then be claimed by the company from the delinquent director. Where such a claim is no longer possible, the company may in the alternative claim any profits which the director may have made as a result of the breach or damages in respect of any loss it may have suffered thereby.’

## Adoptions of the Enlightened Shareholder Value Model

Intense debates preceding the Act’s finalisation saw discussion of different models of a company’s (and, therefore, its directors’) duties and responsibilities. The model adopted by the Act is the so-called ‘enlightened shareholder value model’. This model dictates that directors must place the interests of shareholders first but also holds that, in pursuing shareholders’ best interests in the long term, the interests of all other stakeholders, including employees, suppliers and creditors, as well as the environment and the community at large, must be considered. The ‘triple bottom line’ concept – that it is good for business for companies to be good corporate citizens and to consider social, environmental and economic interests – has now been adopted by the Act.

The SA government’s stated approach was that, in developing new companies’ legislation, it would be guided by a legislative framework that ‘reflects the recognition that the company is a social as well as an economic institution, and accordingly that the company’s pursuit of economic objectives should be constrained by social and environmental imperatives’.

Although government has embraced the enlightened shareholder value model, it has not legislated on the specifics as to what a director’s duty to act in the company’s best interests means. Instead, government has chosen to leave it to our courts to determine the ambit of directors’ duties through the development of our common law. It also concluded that the manifestation of the enlightened shareholder value model in various new provisions of the Act, particularly those which give stakeholders significant new rights and remedies, coupled with the rights and remedies given to stakeholders by numerous other statutes, provided sufficient protection for them.

The Act gives significantly greater rights and remedies to stakeholders, including minority shareholders, and thus encourages stakeholder activism. Two of the most striking – even alarming in some instances – aspects of the Act are:

---

the number of remedies it provides, in particular the number of remedies it provides to minority shareholders, employees and directors; and

---

the number of methods by which its remedies may be enforced. In both of these respects, the Act generally goes further than the companies’ legislation of other western countries, including the USA and the UK.

---

## The codified duties of directors

For the first time, the duties of directors under the common law have been partially codified in sections 75 and 76 of the Act. These partially codified duties prevail over any conflicting common law duties. If there is no such conflict, the common law remains applicable. In most respects, the common law duties of directors have not been altered by this codification to the detriment of directors. Quite the opposite, in fact – the codified duties of directors are more lenient than those of the common law in some important instances.

For this purpose, the meaning of ‘director’ has been expanded to include an alternate director, a prescribed officer, a member of a board committee or a member of the company’s audit committee. These persons are thus bound to observe the same as those duties of directors.

### 1. STANDARDS OF DIRECTOR’S CONDUCT

Section 76(3) codifies what are generally regarded as the most important common law duties of directors. It provides that, subject to sections 76(4) and (5), a director, when acting in that capacity, must exercise the powers and perform the functions of director:

(a) in good faith and for a proper purpose;

(b) in the best interests of the company; and

(c) with the degree of care, skill and diligence that may reasonably be expected of a person (i.e., an objective test)

(i) carrying out the same functions in relation to the company as those carried out by that director (i.e., a person who does the same job as that director, another objective test. This is not a common law requirement and imposes a stricter duty on directors which the common law usually reserves for professionals such as doctors, namely to ensure that they are adequately qualified and experienced to perform their functions); and

(ii) having the general knowledge, skill and experience of that director. (i.e., a subjective test, which reflects the common law position. A director need only meet the standard of knowledge, skill and experience that is expected of a person having the same knowledge, skill and experience as that particular director, no matter how good or bad it may be.)

These standards of conduct are, however, significantly ameliorated by sections 76(4) and (5).

### 2. THE BUSINESS JUDGEMENT TEST

Section 76(4)(a) contains what may well prove to be the most frequently invoked defence by a director when faced with an allegation that the director has breached his duties to the company. It is a statutory version of the so-called ‘business judgement test’, which originated in the USA. It provides that, in respect of any particular matter arising in the exercise of the powers or the performance of the functions of director, a particular director will be deemed to have acted in the company’s best interests and to have performed his functions with the necessary care, skill and diligence in respect of a particular matter (i.e., a director will be deemed to have discharged all the duties set out in section 76(3), other than the duty to act in good faith and for a proper purpose), if the director:



(i) has taken reasonably diligent steps to become informed about the matter. This is an objective test; there is no additional subjective element to it as there is in section 76(3)(c)(ii). This lowers the standard of a director's conduct; and

(ii) either had no material personal financial interest in the subject matter of the decision or disclosed such personal financial interest to the board or shareholders in compliance with section 75; and

(iii) made a decision, or supported the decision of a committee or the board, with regard to that matter. The director is therefore required to actually take a decision. The test does not cover passive acts, such as an abstention from voting; and

(iv) had a rational basis for believing, and did believe, that the decision was in the best interests of the company. This really amounts to a defense against a claim that a director has breached his duty of care and skill (but not his duty of diligence). It effectively lowers the standard of care and skill required of a director at common law from 'reasonableness' to 'rationality', a significant difference, especially when read with section 76(5) (see below).

In short, if a director who has no financial conflict of interest in a matter takes reasonable steps to become informed of the matter but nevertheless, and in good faith, then makes an incorrect decision in relation to it, the director cannot be held liable for contravening sections 76(3)(b) or (c) if there was a rational basis for his decision.

The rationale for the business judgement test is that, since all businesses have to take some financial risk in order to grow and prosper, directors should be encouraged to take carefully considered, reasonable risks, and should not have to worry about being held personally liable for doing so.

### 3. RELIANCE ON OTHERS

Sections 76(4)(b) and 76(5) are largely a codification of the common law in relation to reliance by directors on the actions and information of others in discharging their duties.

Section 76(4)(b) provides that, in respect of any particular matter arising in the exercise of the powers or the performance of the functions of a director, a particular director of a company is entitled to rely on:

(i) the performance by any of the persons referred to in section 76(5) or persons to whom the board may reasonably have delegated, formally or informally by course of conduct, the authority or duty to perform one or more of the board's functions that are delegable under applicable law; and

(ii) any information, opinions, recommendations, reports or statements, including 'financial statements' and other financial data, prepared or presented by any of the persons specified in section 76(5).

Section 76(5) provides that, to the extent contemplated in section 76(4)(b), a director is entitled to rely on:

(a) one or more employees of the company whom the director reasonably believes to be reliable and competent in the functions performed or the information, opinions, reports or statements provided; or

(b) legal counsel, accountants or other professional persons retained by the company, the board or a committee as to matters involving skills or expertise that the director reasonably believes are matters within the particular person's professional or expert competence or as to which the particular person 'merits confidence'; or

(c) a committee of the board of which the director is not a member, unless the director has reason to believe that the actions of the committee do not 'merit confidence'.

Section 76(5) could be used as a barometer against which the standard of skill, care and diligence required of a director in terms of section 76(3)(c) is measured.

### 4. OTHER FIDUCIARY DUTIES

Section 76(2)(a) codifies two common law fiduciary prohibitions or 'negative duties'. It provides that a director of a company must not use the position of director, or any information obtained while acting in the capacity of a director to:

(i) gain an advantage for the director, or for another person other than the company or a wholly-owned subsidiary of the company; or

(ii) knowingly cause harm to the company or a subsidiary of the company.

The references to a 'subsidiary' expand the scope of these common law duties because a director owes no common law fiduciary duty to a subsidiary, whether wholly-owned or not.

Section 76(2)(b) reflects a director's common law fiduciary duty to disclose information which is material to the company. It provides that a director must communicate to the board at the earliest practicable opportunity any information that comes to the director's attention, unless the director:

(i) reasonably believes that the information is immaterial to the company or that the information is generally available to the public, or known to the other directors; or

(ii) is bound not to disclose that information by a legal or ethical obligation of confidentiality.

The expressions 'reasonably believes' and 'ethical obligation' may prove to be significant defences for recalcitrant directors.

## Liability of Directors

### WHAT ARE THE SPECIFIC LIABILITIES THAT DIRECTORS MAY HAVE?

Section 77 codifies the common law liabilities of directors. It also consolidates most of the other sections of the Act which render directors personally liable for losses sustained by the company.

#### 1. COMMON LAW LIABILITIES OF DIRECTORS

Section 77(2) codifies the common law position. It provides that a director may be held liable in accordance with the principles of the common law relating to:

(a) breach of a fiduciary duty, for any loss, damages or costs sustained by the company as a consequence of any breach by the director of a duty contemplated in section 75 (duty to disclose conflicts of financial interests), section 76(2) (the corporate opportunity rule or knowingly causing harm to the company or failure to disclose material information) or section 76(3)(a) or (b) (duties to act in good faith and for a proper purpose, and in the best interests of the company); or

(b) delict (being the law governing wrongful or unlawful acts or omissions) for any loss, damages or costs sustained by the company as a consequence of any breach by the director of a duty contemplated in section 76(3)(c) (duty to exercise care, skill and diligence), any provision of the Act not otherwise mentioned in section 77 or any provision of the company's MOI.

#### 2. STATUTORY LIABILITIES OF DIRECTORS

Section 77(3) provides that a director of a company is liable for any loss, damages or costs sustained by the company as a direct or indirect consequence of the director having:

(a) acted in the name of the company, signed anything on the company's behalf, or purported to bind the company or authorise the taking of any action by or on behalf of the company, despite knowing that the

director lacked the authority to do so; or  
(b) acquiesced in (i.e., tacitly agreed to) the carrying on of the company's business despite knowing that it was being conducted in a reckless, with grossly negligent or fraudulent manner; or

(c) been a party to an act or omission by the company despite knowing that the act or omission was calculated to defraud a creditor, employee or shareholder of the company, or had another fraudulent purpose; or

(d) signed, consented to, or authorised, the publication of:

(i) any financial statements that were false or misleading in a material respect; or

(ii) a prospectus that contained an 'untrue statement' or a statement to the effect that a person had consented to be a director of the company when no such consent had been given,

despite knowing that the statement was false, misleading or untrue, as the case may be.

Knowledge on the part of a director is a requirement of each of these provisions. The words 'knowing', 'knowingly' or 'knows' are defined in section 1 of the Act.

Most of the above actions or omissions are also criminal offences. These are regarded by the Act as the most serious breaches of a director's duties because they are also the only offences that are punishable by a fine or imprisonment of up to 10 years, or both.

Section 77(3)(e) provides that a director is liable for any loss, damages or costs sustained by the company as a direct or indirect consequence of the director having been present at a meeting of directors, and having failed to vote against:

(i) the issuing of any unauthorised shares, despite knowing that those shares had not been authorised in accordance with the Act;

(ii) the issuing of any authorised securities, despite knowing that the issue of those securities was inconsistent with the Act;

(iii) the granting of options to any director, despite knowing that any shares for which the options could be exercised or into which any securities could be converted had not been authorised in terms of the Act;

(iv) the provision of financial assistance to any director for the acquisition of the company's securities, despite knowing that the provision of financial assistance was inconsistent with the Act or the company's MOI;

(v) the provision of financial assistance to a director for a purpose contemplated in the Act, despite knowing that the provision of financial assistance was inconsistent with the Act or the company's MOI;

(vi) subject to the Act, a resolution approving a distribution, despite knowing that the distribution was contrary to the Act;

(vii) the acquisition by the company of any of its shares, or the shares of its holding company, despite knowing that the acquisition was contrary to the Act; or

(viii) an allotment of securities by the company, despite knowing that the allotment was contrary to the Act.

Again, knowledge on the part of the director is a requirement of each of these provisions. These are the more serious contraventions of the Act which a director may commit to which criminal liability does not attach.

Section 77(6), also new, provides that the liability of a person in terms of section 77 is joint and several with any other person who is or may be held liable for the same act. This reinforces the legislature's intention to ensure that a director or prescribed officer who breaches his duties as such pays the maximum legally permissible monetary compensation.

In addition, section 161(1)(b) entitles a securities holder to apply to a court for any appropriate order necessary to rectify any harm done to the securities holder by any director to the extent that the director is or may be held liable in terms of section 77. This widens the scope of civil liability and appears to override the derivative action.

Directors may also be held personally liable under section 218(2), a catch-all provision which states that 'Any person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention.'

### 3. WHAT DEFENCES ARE PERMITTED?

In addition to the business judgment test and the other defences available to a director referred to above, the Act provides for defences which a director may be able to invoke when faced with an alleged contravention of section 77.

If the board of a company has made a decision in a manner that contravened the Act, the company or any director who has been or may be liable under section 77(3)(e) may apply to a court for an order setting aside the decision of the board. The court may make an order setting aside the decision in whole or in part, absolutely or conditionally, and may make any further order that is just and equitable in the circumstances, including an order:

- to rectify the decision, reverse any transaction, or restore any consideration paid or benefit received by any person in terms of the board's decision; and

- requiring the company to indemnify any director who has been or may be held liable in terms of section 77, including indemnification for the costs of the proceedings.

Section 77(9) permits a court, in any proceedings against a director, to relieve the director, either wholly or partly, from any liability set out in section 77, other than for wilful misconduct or wilful breach of trust, on any terms the court considers just, if it appears to the court that:

(a) the director is or may be liable, but has acted honestly and reasonably; or  
(b) having regard to all the circumstances of the

case, including those connected with the director's appointment, it would be fair to excuse the director.

Section 77(9) is a remedy available to a director accused of negligence. Some critics rather cynically refer to section 77(9) as a director's 'get out of jail free card'. It covers virtually the entire spectrum of directors' liabilities, including gross negligence; all that is excluded from its scope is wilful misconduct or wilful breach of trust. It even goes so far as to allow a director to seek relief where the director acted unreasonably. Section 77(9) also overlaps with the business judgment test in section 76(4)(a).

But it does not end there. A director who has reason to apprehend that a claim may be made alleging that the director is liable, other than for wilful misconduct or wilful breach of trust, may apply to court for relief, and the court may grant relief to the director on the same grounds as if the matter had come before the court in terms of section 77(9).

## Persons legally bound by the MOI

Section 15(6) provides, among other things, that a company's MOI is binding between:

the company and each of the company's directors or prescribed officers, in the exercise of their functions within the company; and

the company and any other person serving the company as a member of a board committee, in the exercise of their functions within the company.

These two provisions are new. They override the long-established common law principle that a company's constitution is binding on a company and its shareholders only, and then only in their capacities as shareholders (and not in their capacities as, say, directors, if they are both shareholders and directors). The effect of these two new provisions is that a company (on the one hand) or its directors or board committee members, acting in their respective capacities as such (on the other hand) can now enforce any provision of the MOI or rules against one another in any lawful manner, including the obtaining of an interdict against

the other of them from contravening the MOI or rules, or instituting a monetary claim for damages arising from a breach of the MOI or rules. This approach is consistent with the new derivative action in section 165.

## Requirements for bringing a derivative action against the directors

The new derivative action in section 165 of the Act clearly evidences a trend towards encouraging more aggressive stakeholder activism.

Not only does the Act significantly increase the exposure of directors to personal liability if they do not properly discharge their duties, it also introduces new legal weapons into the arsenal of stakeholders' rights which are far more powerful than they ever had before, two of which are the class action (see below) and the derivative action. The combination of the two may prove to be lethal.

The derivative action is somewhat complex and thus requires a brief explanation: The law regards a company as being a separate legal person. But, of course, a company cannot think for itself; its mind is its board of directors. So, where a company has suffered loss or has been harmed, it is the company's board of directors, and its board alone, which has the power to take remedial action. This often requires a board decision to institute legal or similar proceedings on the company's behalf. In very limited instances, however, a shareholder who believes that legal action should be taken on the company's behalf in circumstances where its board of directors has failed or refused to do so, can apply to court for an order to effectively force the board to do so. This is the common law derivative action.

Section 165 of the Act introduces a codification and streamlining of the derivative action. The new legislation drastically changes the scope, the law and the procedure in relation to derivative actions, all in favour of minority shareholders and other stakeholders, including employees. The result is that directors of companies are now

more exposed to the threat of derivative actions and, as a consequence, personal liability.

The new derivative action is extremely broad in a number of respects. Firstly, the following persons may initiate derivative proceedings:

---

a shareholder or a person entitled to be registered as a shareholder, of the company or of a related company (which includes a holding company, a subsidiary and fellow subsidiaries);

---

a director or prescribed officer of the company or of a related company;

---

a registered trade union that represents employees of the company, or another representative of employees of the company; or

---

a person who has been granted leave of the court to do so, which may be granted only if the court is satisfied that it is necessary or expedient to do so to protect a legal right of that other person.

---

Secondly, the Act broadens the scope of the derivative action considerably by empowering any of the above persons to serve a demand upon a company to commence or continue legal proceedings, or take related steps, against anyone, not just its directors or officers.

Thirdly, the scope of the derivative action is broadened even further because it may now be brought in order to 'protect the legal interests of the company', a very broad expression. The company need not necessarily have sustained damages or loss, or have been deprived of a benefit. 'Legal interests' is not defined. Our courts have consistently given a very wide interpretation to the word 'interests'. There is a clear legal distinction between the words 'rights' and 'interests'. The former means a legally recognised and enforceable claim. The latter means a mere concern, involvement or investment, which could be of a financial, legal, employment or even an environmental nature, to name but a few. The courts will have the unenviable task of defining this term for us. It is likely that derivative actions brought against directors will be based on breach of their

duty of care, skill and diligence, so one would expect the business judgment test to feature prominently.

Fourthly, the Act also provides that all a person must do to commence derivative proceedings is serve a demand on the company to commence or continue the legal proceedings or take related steps. The company (i.e. the board) may apply to court to set aside the demand within 15 business days after it has been served, but only on the very narrow grounds that the demand is 'frivolous, vexatious or without merit'. If the company does not do so or if the court does not set the demand aside, the board must then appoint an independent and impartial person or committee to investigate the demand, and then report to the board on any facts or circumstances that may give rise to a cause of action contemplated in the demand or that may relate to any proceedings contemplated in the demand, the probable costs the company would incur if it pursued such cause of action or continued such proceedings, and 'whether it appears to be in the best interests of the company to pursue any such cause of action or continue any such proceedings'. It is not necessary to apply to court for the appointment of a curator to perform this function.

The board has up to 60 business days (or a longer period as a court, on application by the company, may allow) after being served with the demand to either:

---

initiate or continue legal proceedings, or take related steps to protect the legal interests of the company as contemplated in the demand; or

---

serve a notice on the person who made the demand, refusing to comply with it.

---

A class action may be instituted by way of derivative proceedings. In fact, the Act envisages this very situation by providing in section 165(16), 'for greater certainty', that a person's right in terms of section 165 to serve a demand on a company may be exercised by that person directly, or by another person on that person's behalf, in the manner permitted by section 157. The obvious target for disgruntled stakeholders when things go wrong with a company's business is its board of directors. Take, for example, a situation

where a company decides to retrench some of its employees because it has suffered losses as a result of a board decision to invest in a new business which has subsequently proved to be ill-considered. The class and derivative actions will permit the trade union representing those employees to demand that the company sue all or any of its directors who participated in that decision in their personal capacities for breach of their duties to the company. All the trade union need show is that there may be some merit to the allegation that those directors did not properly discharge their duties. The company will then be forced to appoint an impartial person to investigate the demand, at the company's cost. The consequences for these directors may be disastrous even if the report exonerates them. Apart from having to live with the risk of personal liability, the directors may have to spend up to three months of valuable time and effort dealing with the demand, the negative publicity which the demand may trigger could be extremely harmful to them, and there may be severe disruptions to the company's business. So, directors may well find themselves in precarious positions even if derivative claims against them do not progress beyond the first stage, or even if they ultimately succeed in quashing the derivative claim. They may win the battle but lose the war.

### ARE CLASS ACTIONS PERMISSIBLE UNDER LOCAL LAW?

For the first time, class actions are permitted by section 157(1)(c) of the Act, which states that the right to apply to a court or a regulatory agency under the Act may be exercised by a person 'acting as a member of or in the interests of, a group or class of affected persons'. This alters the firmly entrenched common law rule that a claimant must have a personal and direct interest in the subject matter of the claim.

As section 157(1) clearly indicates, the class action is a legal procedure, not a remedy, its purpose being to give access to justice to people who would be unable to fund the costs of legal proceedings on their own.

If SA follows the trend in the USA, then we could find lawyers willing to take on class action cases at no or little cost to the client in exchange for a percentage of



the amount recovered, and the emergence of businesses that provide funding for class actions on a similar basis. Unfortunately, if overseas experience is followed, the availability of the class action could also result in an increase in litigation activity, which could lead to increases in the premiums on indemnity insurance policies for directors and officers.

Apart from section 157(1)(c), the Act says nothing about the class action. In particular, unlike other countries, it contains no procedural requirements or guidelines for class actions.

## New remedies for Directors

Government has recognised the economic necessity to create and foster investor confidence in South African companies by introducing some significant new rights and remedies for minority shareholders, most of which already exist in similar or modified forms in the company laws of most first world nations. In fact, the Act gives greater powers and enforcement rights to minority shareholders in some respects than they have in the USA and the UK. In line with the enlightened shareholder value approach, the Act also gives other stakeholders, particularly employees, rights and remedies they never had before.

The Act has introduced, among others, the following new remedies for directors:

---

a director may apply to court for relief from abuse of a company’s separate legal personality (i.e., to ‘pierce or lift the corporate veil’) (s20(9));

---

provisions that protect ‘whistle-blowers’ (including directors) who disclose irregularities or contraventions of the Act (s159);

---

a director may apply to a court to have another director declared delinquent or placed under probation (s162); and

---

in certain circumstances, directors may commence or pursue legal action against anyone in the name of the company, via the derivative action (s165).

---

In addition, the so-called ‘minority oppression action’ hasbeen retained in s163 but its scope has been widened considerably.

## Sanctions

The architects of the 1973 Act believed that criminal sanctions would be the most effective deterrent to contraventions of the 1973 Act.

They were wrong. The 1973 Act contained over 120 provisions which levied criminal sanctions. Most of them proved to be ineffective. Unlike the 1973 Act, the Act attempts to balance civil, criminal and administrative sanctions in order to ensure that the sanction, whatever it may be, is the most appropriate and effective in the particular circumstances to which it is applied.

There has thus been a fundamental policy change by Government in that, except for the most serious contraventions and for actions which hinder the administration of the Act, criminal sanctions for contraventions of the Act have been almost entirely replaced by a system of administrative fines and/or civil liability on the part of the offender.

## Procedural issues

### THE STRUCTURE OF THE COURT SYSTEM

The hierarchy of the general courts in SA, in descending order, is the Constitutional Court, the Supreme Court of Appeal, the High Court and the Magistrate’s Courts and lower courts. Most local and international commercial litigation takes place in the High Court or the special courts which have been set up to assist in respect of specialised legal matters, such as the Labour Court, the Land Claims Court, and the Electoral Court, to name but a few. That said, there is nonetheless an increasing number of commercial disputes that are being referred to one of the various alternative dispute resolution mechanisms, such as mediation and arbitration. Furthermore, the Act contains a number of new provisions

which encourage the referral of disputes to alternative dispute resolution.

It should be noted that, on 8 February 2013, an amendment to the South African Constitution was signed which alters the structure of the courts in SA (“Amendment Act”). However, at the time of going to print the date upon which the amendment will come into effect had not yet been determined.

### 1. THE LOWER COURTS AND SPECIAL COURTS

The lower courts, including the Magistrate’s Courts and the Small Claims Court, are often referred to as creatures of statute in that their powers and functions are limited by Acts of Parliament. In terms of the Amendment Act, the Magistrate’s Courts will be renamed “Lower Courts”. The jurisdiction of the lower courts is limited in respect of territorial jurisdiction, monetary jurisdiction and causes of action. For example, the Magistrate’s Courts cannot he ar matters in which the claim exceeds a relatively small amount of money (approximately USD 35,000), unless the parties to the action agree otherwise. The monetary jurisdiction of the Small Claims Courts is even lower (approximately USD 1,500), and only natural persons may institute proceedings in these courts

SA has a number of specialised courts and forums, including the Special Income Tax Courts, the Water Tribunal, the Land Claims Courts, the Labour Courts, the Divorce Courts, the Equality Courts, the Courts for Chiefs and Headman, the Commission for Conciliation, Mediation and Arbitration and the Competition Tribunal.

### 2. THE HIGH COURTS

The High Court of SA currently consists of several regional divisions. Each division has a judge president, one or more deputy judge presidents and as many judges as the President may appoint. The Amendment Act will consolidate the High Courts into a single High Court, with each province having at least one division of the High Court. A High Court may decide any constitutional matter except a matter that may only be decided by the Constitutional Court or that is assigned by statute to another court of a status similar to a High Court. It may

also decide any non-constitutional matter not assigned to another court by statute, including any civil claim.

The High Court has inherent jurisdiction in that the judges have a discretion in regulating proceedings and preventing abuse of court processes. The High Court serves as the court of first instance in respect of all matters that fall outside the jurisdiction of the lower courts and also in cases where a litigant decides to pursue a claim in the High Court, even though the claim falls within the jurisdiction of the lower courts. Generally, a single judge presides when the High Court sits as the court of the first instance in a civil matter. The High Court also serves as a court of appeal. Three judges would generally hear an appeal.

Where a full court sits, the judgment of the majority of the judges is the judgment of the court. If there is no majority judgment, the case will be adjourned and must be heard de novo before a newly constituted court.

### 3. THE COURTS OF APPEAL

Appeals must be noted within a particular period, in accordance with statutory provisions or the provisions of the Rules of Court. The High Court has limited jurisdiction to hear appeals. It may hear any appeal against a judgment or order of an inferior court and a judgment or order of a court constituted before a single judge, provided that the single judge has granted leave to appeal. A litigant can appeal to the Supreme Court of Appeal from the judgment of the High Court sitting as a court of appeal.

Only judgments or orders may be appealed against. Judgments or orders are final in effect, not capable of alteration by the court of first instance, definitive of the rights of the parties, and have the effect of disposing of at least a substantial portion of the relief claimed in the main proceedings.

No judge may sit at the hearing of an appeal against a judgment or order given in a case which was heard before him.

#### 4. THE SUPREME COURT OF APPEAL

The Supreme Court of Appeal ('SCA') consists of the Judge President, a Deputy Judge President and a number of judges. The quorum for a civil appeal is five judges. The judgment of the majority is the judgment of the court. However, if there is no judgment with which the majority of the judges concur, the hearing is postponed and commenced de novo before a new court composed in the manner determined by the Judge President of the SCA, or in his absence, an available senior judge of the Supreme Court of Appeal.

The SCA hears appeals from the High Court. The High Court which heard the matter first must grant leave to appeal. Where such leave is refused, the SCA may grant leave. The High Court or the SCA then directs that the appeal be heard by the full court, unless it is satisfied that the questions of law and of fact and the other considerations involved in the appeal are of such a nature that the appeal requires the attention of the SCA, in which case the appeal would be directly to the SCA.

The SCA is the highest authority in respect of matters which do not have a constitutional element, and its decisions play a leading role in South African commercial litigation. In terms of the Amendment Act, the jurisdiction of the SCA will be narrowed to exclude appeals in respect of labour or competition matters. Consequently, the Labour Appeal Court and the Competition Appeal Court will be the final courts of appeal in such matters, subject only to appeal to the Constitutional Court.

#### 5. THE CONSTITUTIONAL COURT

The Constitutional Court consists of the Chief Justice of SA, a Deputy Chief Justice and nine other judges. A matter before the Constitutional Court must be heard by at least eight judges. The Constitutional Court is the highest court in all constitutional matters and may decide only constitutional matters and issues connected with decisions on constitutional matters.

Once the Amendment Act comes into force, the

Constitutional Court will be the highest court on all issues. It will have the power to hear constitutional matters and any other matter that "raises an arguable point of law of general public importance which ought to be considered by that Court". What is meant by the term "general public importance" in this context and whether it is a separate requirement to a matter "which ought to be considered" will have to be developed by the Constitutional Court.

## Prescription

There are two forms of prescription in South African law, namely acquisitive and extinctive prescription. Both forms are governed by the Prescription Act No. 68 of 1969 (the 'Prescription Act'). Only extinctive prescription is relevant to this paper.

Extinctive prescription is to the effect that a debt, and the creditor's concomitant right of action to enforce that debt, are simultaneously extinguished after the lapse of a certain period of time. Once a debt has prescribed, the debtor is no longer under any obligation to pay that debt, but if the debtor does pay a prescribed debt it cannot reclaim the amount paid. The period of prescription varies according to the type of debt in question. The prescription period for a civil claim is three years, while the prescription period for any judgment debt (excluding foreign judgments) is 30 years.

The period of prescription commences when the 'debt is due'. A debt becomes due only when the creditor has an unconditional right to claim payment and the debtor cannot raise a defence to that claim. So, prescription does not necessarily begin to run when the debt arises.

In terms of section 13 of the Prescription Act, the completion of the period of prescription may be delayed for one year in certain limited circumstances, for example where the creditor is a company and the debtor is a director of such company.

The period of prescription may be interrupted in two ways: by acknowledgement of liability by the debtor (either tacit or express) or by judicial interruption. Even if only part of a debt is acknowledged, the period

of prescription of the whole debt will be interrupted, unless the acknowledgement specifically excludes the inference that the whole debt has been acknowledged. Prescription will also be interrupted by the service on a debtor of any process instituting legal proceedings for the enforcement of a debt, including arbitration. The process instituting legal proceedings will only interrupt prescription if, at the time of service, there was a complete cause of action. Prescription will not be deemed to be interrupted if the creditor does not successfully prosecute his/her claim.

## Enforceability of foreign judgements

### 1. RECOGNITION AND ENFORCEMENT OF FOREIGN JUDGMENTS AT COMMON LAW

While there have been statutory developments in relation to the recognition and enforcement of foreign judgments, most of the law in this regard has been developed by the common law.

The general rule is that a foreign law judgment is not on its own enforceable in SA. However, if a foreign judgment is pronounced on by a proper court of law and certain requirements are met, the determination made therein will be recognised and enforced by a South African court.

It is important to note that, when a South African court decides whether or not to enforce a foreign judgment, it will not pronounce on the merits of the case or on any issues of fact or law already tried by the foreign court and will not review or set aside the foreign court's findings. It will only adjudicate upon whether or not the requirements for enforcement of the judgment have been met.

At common law, there are four requirements that must be met before a South African court will recognise and enforce a foreign judgment:

the foreign court making the judgment must have had 'international competency' or jurisdiction;

---

the foreign judgment must be final and conclusive;

---

the recognition and enforcement of the judgment must not be contrary to South African public policy; and

---

the recognition and enforcement of the judgment must not fall foul of section 1 of the Protection of Businesses Act of 1978. Simply put, this section requires a person seeking to enforce a foreign judgment to obtain permission to do so from the Minister of Trade and Industry in certain circumstances.

---

### 2. ENFORCEMENT OF THE FOREIGN CIVIL JUDGMENTS ACT NO. 32 OF 1988

This Act was enacted in an attempt to overcome the cumbersome common law proceedings. In terms of this Act, it is possible to enforce specified foreign judgments for money claims simply by registering the foreign judgment with a South African court. Where a judgment has been given against any person in a designated country outside SA, such judgment should be lodged with the clerk of the Magistrate's Court of the district where the judgment debtor resides, carries on business or is employed or owns immovable property. The clerk of the court must then register such judgment and issue a notice to the judgment debtor informing him of such registration. This notice must then be served on the judgment debtor by the judgment creditor. This notice also operates as an interdict/injunction against the judgment debtor, and against any person having knowledge of such notice, not to remove or dispose of any assets of the judgment debtor if such removal or disposal would prejudice the execution of the judgment.

Where a judgment has been registered as above, it has the same effect as a civil judgment of the court at which the judgment has been registered.

At present, only Namibia has been chosen as a designated country in terms of this Act.

South African courts will not recognise or enforce a foreign judgment of a revenue or penal nature.

### 3. PROCEDURE FOR ENFORCING A FOREIGN JUDGMENT

In summary, a foreign judgment may be enforced in a

number of ways, the most common of which are:  
instituting an ordinary action based on the foreign judgment as the cause of action;

---

instituting provisional sentence proceedings, if the foreign judgment constitutes a 'liquid document'; or

---

applying to court for a declaratory order in relation to the foreign judgment.

---

Should the action procedure option be followed, the following should be taken into account:

---

allegations that all of the requirements for enforcement of a foreign judgment have been met should be made in the particulars of claim, along with any statements of fact that tend to support such allegations;

---

a certified copy of the foreign judgment should be annexed to the summons; and

---

all necessary foreign documentation should be authenticated in terms of the South African rules of court.

## Insurance of Directors' and Officers' liability

IS DIRECTORS AND OFFICERS' LIABILITY INSURANCE PERMISSIBLE OR LEGAL UNDER LOCAL LAW?

D&O insurance has been permitted in SA for many years. In fact, the Act expressly permits a company to purchase insurance to protect a director against any liability or expenses for which the company is permitted to indemnify a director under the Act.

Insurance in SA is regulated mainly by two statutes, namely the Long Term insurance Act, No. 52 of 1998 and the Short Term Insurance Act, No. 53 of 1998 (the 'STI Act'). The latter Act (read with the Act) governs D&O insurance, which is classified as forming part of liability insurance. South African short term insurance law, including its jurisprudence, is based mainly on English law. Short term insurance is also regulated by a number of other statutes, such as the Financial Advisers Advisory and Intermediary Services Act, No. 37 of 2002. The regulator of the STI Act is the Registrar of Short Term Insurance, who falls under the auspices of the Financial Services Board ('FSB').

CAN AN INSURER WRITE D&O INSURANCE ON A NON-ADMITTED BASIS?

As long as an insurer is registered as a short term insurer in terms of the STI Act, it may write D&O insurance. No additional license is required to do so. However, an insurer cannot write D&O insurance on a 'non-admitted' basis; section 7(1) of the STI Act prohibits a person from carrying on any kind of short term insurance business unless the person is registered as a short term insurer. There is one exception – Lloyd's underwriters are authorised by the Act itself to carry on short term insurance business. The law is silent on the freedom of buyers to purchase insurance outside SA but the FSB has issued a directive on the subject, which contains a number of procedural requirements that must be met

for South African residents to purchase insurance from non-admitted carriers. It is also permissible to belong to a global programme but an application must be made to the South African Reserve Bank for the cross border remittance of premiums to non-admitted insurers.

Section 78 of the Act governs D&O liability and insurance. For this purpose, the meaning of 'director' has been expanded to include a former director, an alternate director, a prescribed officer, a board committee member or an audit committee member, irrespective of whether or not the person is also a director.

Section 78(2) provides that, subject to sections 78(4) to (6), any provision of an agreement, the MOI or rules of a company, or a resolution adopted by a company, whether express or implied, is void to the extent that it directly or indirectly purports to:

(a) relieve a director of a duty contemplated in sections 75 or 76 (see above), or of liability contemplated in section 77 (see above); or

(b) negate, limit or restrict any 'legal consequences' arising from an act or omission that constitutes wilful misconduct or wilful breach of trust on the part of the director.

In other words, a director cannot contract out of his common law or statutory duties or liabilities, but the 'legal consequences' of an unlawful act or omission (whatever they may be, including the amount of damages for which the director may be held liable) may be negated, limited or restricted by agreement (such as an insurance contract) in all instances, other than where the act or omission constituted wilful misconduct or wilful breach of trust on the part of the director.

The Act goes on to provide in section 78(4) that, unless its MOI provides otherwise, a company may advance expenses to a director to defend litigation in any proceedings arising out of the director's service to the company. A company may not, however, directly or indirectly pay any fine that may be imposed on a director as a consequence of that director having

been convicted of an offence, nor may a company indemnify a director in respect of such a fine, unless the conviction was based on strict liability. In addition to being able to advance such expenses to a director, a company can (again, unless its MOI provides otherwise) directly or indirectly indemnify a director for such expenses. However, such an indemnity is valid only if the proceedings:

---

are abandoned or exculpate the director; or

---

arise in respect of any liability for which the company may indemnify the director in terms of sections 78(5) and (6) (see below).

Sections 78(5) and (6) provide that, unless its MOI provides otherwise, a company may indemnify a director in respect of 'any liability arising', an extremely broad expression which undoubtedly encapsulates defense costs. They seem to mean 'any liability arising out of a director's services to the company'. It is, therefore, not surprising that there are some exceptions to this blanket indemnity, namely that a company may not indemnify a director in respect of:

(a) any liability arising from the director having:

(i) acted in the name of the company, signed anything on behalf of the company, or purported to bind the company or authorise the taking of any action by or on behalf of the company, despite knowing that the director lacked the authority to do so; or

(ii) acquiesced in the carrying on of the company's business despite knowing that it was being carried on recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose; or

(iii) been a party to an act or omission by the company despite knowing that the act or omission was calculated to defraud a creditor, employee or shareholder of the company, or had another fraudulent purpose; or

(b) any liability arising from wilful misconduct or wilful breach of trust on the part of the director; or



(c) any fine imposed on a director as a consequence of that director having been convicted of an offence, unless the conviction was based on strict liability.

A company may therefore indemnify a director in respect of any liability arising from that director's negligence. A company may also indemnify a director in respect of the costs incurred by the director in defending a claim against that director for negligence or any other liability (save for the limited exceptions in section 78(6)) arising from that director's service to the company.

Section 78(7) is the only provision of the Act which deals specifically with D&O insurance. It provides that, unless its MOI provides otherwise, a company may purchase insurance to protect:

(a) a director against any liability or expenses for which the company is permitted to indemnify a director in accordance with section 78(5); or

(b) the company against 'any contingency' including, but not limited to:

(i) any expenses that the company is permitted to advance in accordance with section 78(4) or for which the company is permitted to indemnify a director in accordance with section 78(4); or

(ii) any liability for which the company is permitted to indemnify a director in accordance with section 78(5).

Accordingly, the Act expressly permits D&O insurance to cover a director for negligence as well as for costs incurred by the director in defending litigation arising from the director's service to the company, except for the limited exceptions set out in section 78(6). Defense costs are invariably included in the insurer's liability since it is usually the insurer which has the obligation to defend and contest any claim made against the director. A company is now permitted to take out D&O insurance against most contingencies at its cost, even if the director receives the proceeds of the policy. This was not permitted under the 1973 Act. In particular, D&O insurance may be taken out for breach by a director of

a director's duty under sections 75 and 76.

**ARE CLAIMS MADE AND REPORTED POLICIES PERMISSIBLE UNDER LOCAL LAW, OR DOES THE LAW REQUIRE OCCURRENCE?**

All D&O insurance in SA is structured on a 'claims made and reported' basis, which is a fundamental principle of SA's common law of insurance and has been the subject of numerous judgments by our courts.

## Claims brought directly against the insurer

As a general rule, claims cannot be brought directly against the insurer of a director and officer because it is usually the case that the company is the policyholder while the director is the insured.

**ON WHAT GROUNDS CAN THE INSURANCE BE AVOIDED/RESCINDED?**

The insurer under a D&O insurance policy may avoid or rescind a claim on certain grounds, the most prevalent being non-payment of premiums (i.e., default or breach of the policy) or material non-disclosure. A policy is, however, not invalidated on account of any misrepresentation or disclosure made to the insurer unless that representation or disclosure is such as to be likely to materially affect the assessment of the risk under the policy concerned at the time of its issue or renewal (s53(1) of the STI Act).

## Severability

Severability of a D&O policy is permissible. Invariably, a D&O policy provides that the policy covers every insured for his/her own individual interest.

If a local company is a subsidiary of a foreign parent and such foreign parent had a worldwide D&O policy which covers the local subsidiary, is a separate local D&O policy required to be issued for such subsidiary to comply with local law?

A South African D&O policy is not required to be issued where a foreign holding company of a South African subsidiary has a worldwide D&O policy which covers SA, unless the South African subsidiary pays the premiums.

## Claims history

SA does not have a history of large D&O insurance claims, but it is nevertheless common practise among large companies, in particular listed companies, to purchase D&O insurance. SA has experienced very few claims arising out of the United States of America ('USA') or based on US law. It is nonetheless common practise to exclude from a D&O policy claims arising out of any US claim, with certain exceptions.

## Extended reporting period/discovery in local law

There are no special laws with regard to an insurer having to offer an extended reporting period/discovery, though it is common practice to do so.

**We wish to gratefully acknowledge the assistance of Angela Jack: Divisional Director: Executive Liabilities, Marsh Africa in drafting this paper.**

**CARL STEIN**

Director: Bowman Gilfillan Inc.

**DONOVAN WESTBROOK**

Associate: Bowman Gilfillan Inc.

**BG** Bowman Gilfillan  
AFRICA GROUP

**Antananarivo**

Tel +261 20 224 3247  
Fax +261 20 224 3248  
Email [info@jwfllegal.com](mailto:info@jwfllegal.com)  
[www.jwfllegal.com](http://www.jwfllegal.com)

**Cape Town**

Tel +27 21 480 7800  
Fax +27 21 480 3200  
Email [cpt\\_info@bowman.co.za](mailto:cpt_info@bowman.co.za)  
[www.bowman.co.za](http://www.bowman.co.za)

**Dar es Salaam**

Tel +255 22 277 1885  
Fax +255 22 277 1886  
Email [info@ealc.co.tz](mailto:info@ealc.co.tz)  
[www.ealawchambers.com](http://www.ealawchambers.com)

**Gaborone**

Tel +267 391 2397  
Fax +267 391 2395  
Email [info@bookbinderlaw.co.bw](mailto:info@bookbinderlaw.co.bw)  
[www.bookbinderlaw.co.bw](http://www.bookbinderlaw.co.bw)

**Johannesburg**

Tel +27 11 669 9000  
Fax +27 11 669 9001  
Email [info@bowman.co.za](mailto:info@bowman.co.za)  
[www.bowman.co.za](http://www.bowman.co.za)

**Kampala**

Tel +256 41 425 4540  
Fax +256 31 226 3757  
Email [afmpanga@afmpanga.co.ug](mailto:afmpanga@afmpanga.co.ug)  
[www.afmpanga.co.ug](http://www.afmpanga.co.ug)

**Nairobi**

Tel +254 20 289 9000  
Fax +254 20 289 9100  
Email [ch@coulsonharney.com](mailto:ch@coulsonharney.com)  
[www.coulsonharney.com](http://www.coulsonharney.com)

Member

**LexMundi**  
World Ready

Lex Mundi is the world's leading network of independent law firms with in-depth experience in 100+ countries worldwide.