

**CORPORATE GOVERNANCE AND CORPORATE COLLAPSE
THE FAILURE OF STEINHOFF**

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A thesis submitted in fulfilment of the requirements for the degree

Doctor of Laws

in the
Department of Mercantile Law
Faculty of Law
University of the Free State
Bloemfontein

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Date 29/07/2023

DECLARATION

I, Hyla Magdalena De Kock, declare that the thesis that I herewith submit for the doctoral degree, Doctoral of Laws, at the University of the Free State, is my independent work and that I have not previously submitted it for a qualification or another institution of higher education.

I also declare that no work of other scholars has been used without the means of proper citation and that all sources I have used or quoted have been indicated and acknowledged by means of complete reference.



.....
HM DE KOCK

29-07-2023
Date

DEDICATION

To my late husband, Jan Albert de Kock and my family for their continuous support in completing my thesis.

ACKNOWLEDGEMENTS

I am grateful to Prof Elizabeth Snyman-Van Deventer, my promoter, for her assistance, contributions and unwavering support during every stage of the research project. I managed to complete this work because she did not only provide academic support, but she became my support system. Thank you Prof.

I would like to express my gratitude to the staff at the Department of Mercantile Law for their support.

ABSTRACT

This research will evaluate the corporate governance practices of Steinhoff International Holdings N.V. from December 2017, when the scandal started, until 30 April 2023. The assessment contains several newspaper articles that reflected the timeline of the events as they unfolded. The annual reports of Steinhoff are the most important documents that were produced by the company reflecting the corporate governance policy and practices during a specific financial year.

The research aims to examine the role of corporate governance measures in South African company law to prevent future corporate collapses. The failure of Steinhoff International N.V.¹ ("Steinhoff") will serve as a case study to indicate the success or failure of corporate governance measures in South Africa. This study investigates corporate governance and the board of directors' responsibilities in South African companies with specific reference to Steinhoff to investigate whether the directors of Steinhoff fulfilled these responsibilities. Therefore, the thesis's primary objective is to investigate and evaluate corporate governance measures and interventions in order to determine why the measures do not prevent corporate collapses. Secondly, the thesis aims to evaluate legislation and other measures in South Africa, Germany, Australia and the United States of America to make recommendations for preventing future corporate catastrophes. The global corporate governance failures were severe. It seems as if fraud and corruption may be the major sources of these corporate collapses. In most instances, there is either the active involvement of the directors and managers in these fraudulent or corrupt practices, or there is either a negligent or even intentional failure to act by directors to prevent these activities.

The study shows that the prevention of corporate failure remains a complex endeavour. Legislation, codes of conduct, structures, and processes cannot resolve all problems on their own. The ethical and responsible behaviour of company directors, managers, and officers is crucial. Regardless of the outcome of any legal proceedings, the collapse of

¹ As stated in Steinhoffs' Annual report 2022:3 "*Steinhoff International Holdings N.V. is a public limited liability company (naamloze vennootschap) incorporated under the laws of the Netherlands, with its corporate seat in Amsterdam, the Netherlands, and its principal place of business at Building B2, Vineyard Office Park, Cnr Adam Tas & Devon Valley Road, Stellenbosch 7600, South Africa. The Company is registered with the Trade Register in the Netherlands under number 63570173, LEI code 724500PSNX8EVPOZ1M58 and has tax residency in South Africa.*"

Steinhoff demonstrates the crucial role of the companies' board, company secretary, auditors, directors, shareholders, and other stakeholders in assuring compliance with all applicable legislation and it operates with integrity and transparency. I believe that, similar to Enron, Steinhoff will become the new benchmark for corporate governance failures.

Keywords: corporate governance, corporate collapse, Steinhoff collapse, Companies Act 71 of 2008, King reports,

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LIST OF ABBREVIATIONS AND ACRONYMS

AFU	Asset forfeiture unit
ASIC	Australian securities and investment commission
ASX	Australian Stock Exchange
APPENDIX 4 G-form	Key to disclosures Australian corporate governance councils' principles and recommendations
BJR	Business judgment rule
CIPC	Companies and intellectual property commission
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CODE-	Code of best practice
COMMITTEE	The Cadbury committee
Companies Act 71 of 2008	
Competition Act 89 of 1998	
DPCI	Directorate of priority crime investigation
Dti	Department of Trade and Industry
FIC	Financial Intelligence Centre
FSCA	Financial Sector Conduct Authority
FSE	Frankfurt Stock Exchange
GAAP	General accepted accounting practice
GEPF	Government Employees Pension Fund
Guidelines	Dti guidelines for corporate law reform
IoD	Institute of Directors of Southern Africa
IRBA	Independent Regulatory Board for Auditors
JSE	Johannesburg Stock Exchange
King I	King I report 1994
King II	King II report 2002
King III	King III report 2009 entitled the King Report on Corporate Governance for South Africa and the King Code of Governance Principles

King IV	King IV report 2016
NPA	National Prosecuting Authority
NYSE	New York Stock Exchange
OECD	Organisation for Economic Co-operation and Development
PAIA	Promotion to Access to Information Act 2/2000
PIC	Public Investment Company
PWC	Price Waterhouse Coopers
SARB	South African Reserve Bank
SE	Societas Europaea
SEC	Securities And Exchange Commission
Securities Services Act 36/2004	
SIHNV	Steinhoff International Holdings N.V.
SRI	Socially Responsible Investment
STEINHOFF	Steinhoff International Holdings in South Africa
SCOF	Standing Committee On Finance
SCOPA	Standing Committee On Public Accounts
SOX	Sarbanes-Oxley Act of 2002
UK	United Kingdom
USA	United States
VEB	Dutch Vereniging van Effectenbezitte

CHAPTER 1: INTRODUCTION

1 INTRODUCTION

This chapter will set out the preliminary research issues. It will explain the research problems within the broader context of the recurring corporate collapses in South Africa and internationally. It will raise the fundamental questions that inform the research, define the scope of the research, and identify the objectives and significance of the research methodology employed in conducting the research.

2. STATEMENT OF THE PROBLEM

The purpose of this study is to examine the role of corporate governance measures in South African company law to prevent future corporate collapses. The failure of Steinhoff International N.V.² ("Steinhoff") will serve as a case study to indicate the success or failure of South African corporate governance measures.

3. RESEARCH QUESTIONS

Do the current governance systems in companies reflect good governance as envisaged by codes and legislation enacted to govern companies? This study investigates corporate governance and the responsibilities of the boards of directors in South African companies with specific reference to Steinhoff to investigate whether the directors of Steinhoff fulfilled these responsibilities.

Based on the above, the research intends to answer the following sub-questions:

² As stated in Steinhoffs' Annual report 2022:3 "*Steinhoff International Holdings N.V. is a public limited liability company (naamloze vennootschap) incorporated under the laws of the Netherlands, with its corporate seat in Amsterdam, the Netherlands, and its principal place of business at Building B2, Vineyard Office Park, Cnr Adam Tas & Devon Valley Road, Stellenbosch 7600, South Africa. The Company is registered with the Trade Register in the Netherlands under number 63570173, LEI code 724500PSNX8EVPOZ1M58 and has tax residency in South Africa.*"

- 3.1 Who is ultimately accountable for corporate governance?
- 3.2 How effective are the measures and regulations of the common law, the Companies Act 71 of 2008, and the King Reports in preventing corporate collapses?
- 3.3 What were the reasons for the collapse of Steinhoff?
- 3.4 What measures can be put in place to prevent corporate collapse?

4. AIM AND OBJECTIVES

Therefore, the primary objective of the thesis is to investigate and evaluate corporate governance measures and interventions in order to determine why the measures do not prevent corporate collapses. The secondary objective of the thesis is to evaluate legislation and other measures in South Africa, Germany, Australia, and the United States in order to make suggestions for preventing future corporate collapses.

The corporate governance structures, external regulatory bodies, and enforcement of these governance principles influence corporate governance and corporate design.³ The failure of corporate governance was probably not the primary cause of the financial collapse of Steinhoff. Still, good corporate governance may have insulated and mitigated the impact and consequences of the financial implosion.

5. SIGNIFICANCE OF THE RESEARCH

Since 2000 the corporate governance collapses worldwide were severe. It seems as if fraud and corruption may be the major sources of these corporate collapses. In most instances, there is either the active involvement of the directors and managers in these fraudulent or corrupt practices, or there is either a negligent or even intentional failure to act by directors to prevent these activities.

³ Winter 2011:2.

In the USA, several companies like Enron,⁴ Worldcom,⁵ Sprint,⁶ AbbVie,⁷ Imclone,⁸ Global Crossing,⁹ and Tyco International¹⁰ suffered significant financial losses due to substantial fraudulent misstatements and other illegal, corrupt, or unethical practices. Executives were, in some instances, convicted of fraud and sentenced to prison. The Sarbanes-Oxley Act was enacted as a result of these corporate financial scandals and governance failures, as well as the subsequent public outcry.¹¹ In the European corporate scandals involving Parmalat¹² (Italy), Royal Dutch Ahold¹³ (Netherlands), Vivendi¹⁴ (France), Adecco¹⁵ (Switzerland) and Elan¹⁶ (Ireland), the boards failed to identify financial misrepresentations.¹⁷ However, none of these controversies resulted in mandatory

⁴ Uberoi 2018:3-4; Wallace 2003:96; Wade 2002:100; Owen 2003: 169-170; Radin 2007:370. Thompson 2003:102 the corporate collapse of India's Satyam Computer Services is regarded as "India's Enron" wherein a lack of transparency, accountability and lack of oversight on the part the board of directors of the company resulted in accounting fraud and ultimately the collapse of India's most successful software company.

⁵ Wallace 2003:103; Mmadu 2013:25; Owen 2003 170; Radin 2007: 370. WorldCom collapse involved accounting irregularities wherein earnings were inflated.

⁶ Mmadu 2013:25; <https://edition.cnn.com/2020/08/03/tech/sprint-mobile-brand/index.html#:~:text=The%20failed%20merger%20left%20Sprint's,out%20of%20at%20this%20point.%E2%80%9D> accessed 17/2/2023. Sprint was on the brink of bankruptcy due to bad management decisions and a merger brought an end to the company.

⁷ <https://www.nytimes.com/2023/01/28/business/humira-abbvie-monopoly.html> accessed 17/2/2023. Through exploitation of the US patent system, the company block competitors and ensures the increase of drug prices.

⁸ Mmadu 2013:25; <https://www.chicagotribune.com/sns-ap-martha-stewart-chronology-story.html> accessed 17/2/2023. The insider trading scandal (made famous because of the involvement of Martha Stewart) in which shares were sold because of fears that the company's cancer drug would be rejected.

⁹ Mmadu 2013:25; Owen 2003: 171. See also <https://www.investopedia.com/terms/g/globalcrossing.asp#:~:text=The%20company%20was%20known%20for,lawsuits%20for%20alleged%20securities%20fraud> Accessed 17/2/2023. Due to aggressive and allegedly fraudulent accounting practices and a potential transaction with Enron that would have inflated each company's respective revenues by \$650 million. In 2004, Global Crossing settled numerous lawsuits for alleged securities fraud.

¹⁰ Wallace 2003:102; Mmadu 2013:25; Owen 2003:171; Radin 2007:370. Tyco International was investigated for self-dealing by insiders and tax evasion.

¹¹ Wallace 2003:101-120.

¹² Parmalat was a typical example of strong managers and unprotected minority shareholders. Dibra 2016:282; Beecher-Monas 2007:379. See also Quinn 2014:58-59.

¹³ Corporate scandals involving Parmalat and Royal Dutch Ahold were ascribed to a wide range of factors, including poor involvement and participation of shareholders, a lack of transparency and inadequate supervision, and reporting failures.

¹⁴ Rosemain 2021:1 The media conglomerate Vivendi's corporate scandal involved false financial statements and a lack of transparency. <https://www.reuters.com/article/us-vivendi-lawsuit-idUSKBN2B10GO> Accessed 01/05/2023.

¹⁵ Lublin and Ascarelli 2004:1 Adecco a North American super mark group, delayed the publishing of its audit report. due to material weaknesses in internal controls. <https://www.wsj.com/articles/SB107388945880551500> Accessed 01/05/2023.

¹⁶ Hearne 2013:1. In periodic reports lodged with the Commission and in quarterly earnings press releases distributed to investors in the United States, the Irish pharmaceutical company Elan failed to disclose material information about the company's financial results. <https://www.irishexaminer.com/lifestyle/arid-20240094.html> Accessed 01/05/2023.

¹⁷ Winter 2011:3; Beecher-Monas 2007:373.

legislation, the notion of "comply or explain" was used as the basis for the development of only state-level corporate governance codes.¹⁸

Prevention of business failures is of the utmost significance, especially when one considers the negative effects that result from such failures. In addition to the predicted decrease in share values, there will be repercussions for shareholders, employees, pension funds, creditors, and society.

6. RESEARCH METHODOLOGY

The proposed research will adopt a doctrinal methodology, a subjective, interpretive and argument-based qualitative analysis to arrive at a coherent, consistent outcome with respect to the causes of corporate collapse and prevention thereof.

7. LIMITATIONS OF THIS RESEARCH

This research will evaluate the corporate governance practices of Steinhoff International Holdings N.V. from December 2017, when the scandal started, until 30 April 2023. The assessment contains several newspaper articles that reflected the timeline of the events as they unfolded. The annual reports of Steinhoff are the most important documents that were produced by the company reflecting the corporate governance policy and practices during a specific financial year.

A discussion of the world's various international corporate governance structures is a study on its own. For this reason, the study will present a concise introduction to the corporate governance frameworks of Germany, Australia and the United States. The corporate governance structures and principles of Germany, Australia and the United States on preventing corporate collapse will be compared with those of South Africa. The overview is limited to Germany, Australia and the United States because these countries can be regarded as three of South Africa's main trading partners. Furthermore, Australia and South Africa have the same United Kingdom influences on their company law.

¹⁸ Winter 2011:5-6; Beecher-Monas 2007:372.

8. TERMINOLOGY

The terms company and corporation will be used as equivalent terms.

9. STRUCTURE OF THE RESEARCH

The remainder of this dissertation is structured into the chapters below.

CHAPTER 2

This chapter will concentrate on the origin, sources, and foundation of corporate governance, as well as the nature and forms of corporate failures. In order to appreciate the difficulties of corporate accountability, it will adopt a historical approach. It will also show the dynamics of a modern system of corporate responsibility. The chapter will indicate the various actors responsible for corporate governance in a company. It will explain the application of enhanced transparency as per Chapter 3 of the South African Companies Act¹⁹ ("the Act") and the King I, II, III, and IV reports. The chapter will further examine the key theories of corporate governance and distinguish between the application of corporate governance on the one hand and the effect thereof on the other. After that, the chapter will attempt to identify the challenges emanating from the application of corporate governance.

CHAPTER 3

In this chapter, the business and management structures of Steinhoff as well as the timeline of the collapse of Steinhoff, will be set out. The chapter aims to give an overview of Steinhoff and the timeline to serve as background for the following chapters. Newspaper reports are used as their coverage of the Steinhoff collapse daily, as it gives the unfolding of the collapse within a specific timeframe.²⁰

CHAPTER 4

¹⁹ 71 of 2008.

²⁰ Newspaper reports are used as their coverage of the Steinhoff collapse as it unfolded, and gives the timeframe.

Chapter Four sets out the South African corporate law. It investigates the role and impact of the King Reports and Companies Act 71 of 2008 on corporate governance. The chapter additionally addresses the matter of board composition, as well as the responsibilities of directors, encompassing fiduciary duties, duty of care, and duty of skill. It is followed by an investigation into the business judgment rule. The various stakeholders and stakeholders' interests are also briefly discussed. An additional significant factor in promoting effective corporate governance inside corporations pertains to the involvement of various committees, particularly emphasising the audit committee and the social and ethics committee. The chapter also includes a very brief look at other corporate scandals in South Africa.

CHAPTER 5

This chapter will examine how the governance structure and practices in Steinhoff contributed to the collapse of Steinhoff. It will identify the corporate structures of Steinhoff before and after the collapse. This chapter identifies the reasons for the Steinhoff collapse regarding the prevention of corporate collapse. Corporate governance principles and structures are supposed to ensure sustainable, ethical and business practices. Thus, Steinhoff is an example of how non-compliance and unethical behaviour leads to a company's collapse. International corporate governance structures will be identified and compared with current corporate governance structures to identify how corporate collapse can be prevented. The preventative measures will then be examined to prevent corporate governance collapse.

CHAPTER 6

This chapter aims to identify and compare the corporate governance systems of the United States of America (USA), Germany, and Australia with the existing corporate governance structures of South Africa. However, this thesis does not delve into an extensive analysis of the different corporate governance structures. Instead, it focuses on identifying and comparing corporate governance failures and preventative measures in these different jurisdictions, specifically in relation to South Africa to contribute to finding a solution for

possible future corporate collapses. Specific focus will be on the board, the responsibilities of directors, such as adherence to the business judgement rule, the functions of the audit committee, reporting and disclosure practices, certification obligations, external audit procedures, considerations for both shareholders and stakeholders interests, and a particular emphasis on the principles of sound corporate governance and recommendations for optimal practices in the Australian context.

CHAPTER 7

This chapter will analyze the application of measures to prevent corporate collapse. It will examine the effects and likely challenges that could stand in the way of applying specific measures. This chapter deals with recommended measures and the application of preventative measures for corporate collapse.

CHAPTER 8

This chapter concludes the research with a summary, findings and recommendations. The chapter will be titled and structured as follows:

Conclusion

- 8.1 Summary
- 8.2 Re-visiting the Research Thesis
- 8.3 Observations
- 8.4 Recommendations
- 8.5 Questions for Further Research
- 8.6 Conclusion
- 8.7 Bibliography

CHAPTER 2: BACKGROUND

1. INTRODUCTION

This chapter will focus on the origin, sources, and basis of corporate governance and the nature and forms of corporate collapse. The chapter's first focus will be defining, if possible, corporate governance. It will adopt a historical approach to appreciate the challenges of corporate responsibility. It will also show the dynamics of a modern system of corporate responsibility. The chapter will indicate the various actors responsible for corporate governance in a company. It will explain the application of enhanced transparency as per Chapter 3 of the South African Companies Act²¹ ("the Act") King I, II, III, and IV reports. The chapter will examine the key theories of corporate governance and distinguish between the application of corporate governance on the one hand and the effect thereof on the other. After that, the chapter will attempt to identify the challenges emanating from the application of corporate governance.

2. CORPORATE GOVERNANCE DEFINED

According to Mongalo,²² corporate governance is not a new concept. Shi emphasized it has been practiced since the inception of corporate entities.²³ Tingle explains that the definition of corporate governance has changed over the past four decades.²⁴ Corporate governance now refers to adopting specific legal structures and practices to measure corporate governance.²⁵ As stated by Langeni,²⁶ there is no set definition of corporate governance, but academics have laid down various definitions, as highlighted below. There are generally accepted principles and practices that fall under the auspice of corporate governance, but there is not one universally agreed-upon definition. The

²¹ 71 of 2008.

²² Mongalo 2004:101.

²³ Shi 2007:197.

²⁴ Tingle 2018:222-225.

²⁵ Tingle 2018:227; Shu-Acquaye 2007:584 described corporate governance as some form of company control.

²⁶ Langeni 2018:33.

definition of corporate governance can vary depending on the context, the region, or the organisation in question. Cremers refers to corporate governance as a moving target.²⁷ Additionally, stakeholders may have different perspectives on what constitutes good corporate governance. However, despite the need for a single definition, the importance of corporate governance in ensuring that companies operate responsibly and sustainably is widely recognised.

According to Majmudar, corporate governance is "*the collection of procedures, conventions, policies, laws, and institutions that influence how a business is directed, administered, and regulated.*"²⁸ Bisconti describes corporate governance as where all the corporations' powers are exercised with the approval of the shareholders at the board's discretion because the board of directors is responsible for managing the business and affairs of the corporation.²⁹ Similar to Majmudar, Bisconti's article focused on the board of directors' duties and responsibilities towards the corporation without concentrating on measures to prevent corporate collapse.

Cassim, Kyereboah-Coleman and Prisantani described corporate governance as a performance management system that reduces the risk of major corporate collapse.³⁰ Corporate governance's essential objectives are delegating powers to managers and ensuring transparency, fairness, accountability, and responsibility to all stakeholders.³¹ Lee noted that good corporate governance seeks to balance economic and social goals and two competing corporate values, authority and accountability, the need to preserve the board's decision-making discretion (authority) and the need to hold the board accountable for its decisions.³² Similar to Lee, Rathbone and Kyereboah-Coleman hold that corporate governance is the rules and procedures utilised by the board of directors to ensure accountability by all stakeholders.³³ However, neither Lee, Rathbone, nor Kyereboah-Coleman refers to mechanisms to prevent corporate governance collapse.

²⁷ Cremers et al 2016:747.

²⁸ Majmudar 2021:74.

²⁹ Bisconti 2009:770.

³⁰ Cassim et al 2018:271; Kyereboah-Coleman 2007:22; Prisantani 2019:27.

³¹ Cassim et al 2018:273; Al Shunnaq; and Al Azzam 2018:53.

³² Lee 2005:52; Mongalo 2003:177.

³³ Rathbone 2020:181; Kyereboah-Coleman 2007:18.

Murphy sees corporate governance as a sub-system of decision-making within the corporation.³⁴ Mongalo noted that corporate governance focuses on the entire network of aligning the interests of organisations, stakeholders and society.³⁵ Both Murphy and Mongalo focus on the decision-making process and the alignment of interests; however, the preventative measures of corporate collapse and the effect thereof are not discussed.

Prisandani explained that corporate governance should ensure redress in the event of a violation of minority shareholder rights by majority shareholders.³⁶ Shi averred that every country approaches corporate governance from its cultural background; therefore, corporate governance systems differ worldwide.³⁷ Strine noticed that most European countries' corporate laws expressly state that corporations' managers explicitly have a duty to consider all the stakeholders, not just shareholders, in their company management.³⁸ The German corporate law illustrates this in terms of which managers must take the interests of shareholders, employees, and society as a whole into account in their management of the company.³⁹ In France and the Netherlands, the approach was also that corporate managers are to consider the interests of all constituencies in running the corporation.⁴⁰ I agree with Shi that the corporate governance systems of the USA, Germany and Australia differ from that of South Africa. In South Africa, the corporate governance principles focus on ethical leadership, oversight of management, ethical compliance with laws, regulations and transparency. The importance of effective risk management to achieve sustainability and accountability. The importance of shareholder and stakeholder involvement, thereby recognizing the interests of shareholders and stakeholders

³⁴ Murphy 2008:132.

³⁵ Mongalo 2003:177-179; Prisandani 2020:22.

³⁶ Prisandani 2019:27-28 refers to the Indonesian Company Law.

³⁷ Shi 2007:197-212.

³⁸ Strine 2016:1247.

³⁹ Strine 2016:1247.

⁴⁰ Strine 2016:1247-1248.

The most popular definition, as mentioned by Sir Adrian Cadbury⁴¹ in the Cadbury report,⁴² is that corporate governance is a system whereby companies are directed and controlled.⁴³ This definition was later adopted by the Organisation for Economic Co-operation and Development (OECD).⁴⁴ The OECD describes corporate governance as a director's challenges between performance (driving forward) and conformance (prudent control).⁴⁵

Shi⁴⁶ concurs with the description of the OECD in that corporate governance provides a valuable framework for analysing the key capabilities of directors and the fundamental governance principles of accountability, honesty and transparency that inform board processes.⁴⁷ Similar to the Cadbury committee, Cassim views corporate governance as a management framework consisting of structures and processes within which decisions are made, and companies are controlled.⁴⁸ Schleifer and Vishny⁴⁹ focus on the separation of management and finance. Jacobs asserts that corporate governance is determined by the complexity of the organisation and not according to size.⁵⁰

Adams and Matheson describe corporate governance as a system of contractual and fiduciary duties influencing the company's directors and officers to make decisions consistent with their defined obligations and considering shareholders' interests first when making corporate decisions.⁵¹

A multitude of academics defines corporate governance from a relationship perspective. Dibra focuses on the relationship between management (corporate insiders) and all

⁴¹ Cadbury report 1992:14.

⁴² Wiese 2018:5; Moloï 2008:1; Berle and Means 1991:1; Anonymous 2003:269.

⁴³ <https://www.fin24.com/Opinion/the-steinhoff-saga-part-two-the-board-that-looked-the-other-way-20180628> Accessed 30/1/2019. Dbe 2003:269 noted that corporate governance involves relationships between stakeholders and shareholders. Clarke 2010:78.

⁴⁴ <https://www.oecd.org/corporate/ca/corporategovernanceprinciples/31557724.pdf> Accessed 7/3/2019. Dbe 2003:269. Mongalo 2003:178-191.

⁴⁵ <https://www.oecd.org/corporate/ca/corporategovernanceprinciples/31557724.pdf> Accessed 7/3/2019.

⁴⁶ Shi 2007:197-212 emphasized the accountability by those who are in control of the operations of the corporations.

⁴⁷ <https://www.fin24.com/Opinion/the-steinhoff-saga-part-two-the-board-that-looked-the-other-way-20180628> Accessed 30/1/2019; Prisdani 2019:22; Zhao and Wen 2022:80-81.

⁴⁸ Cassim et al 2019:271; Al Shunnaq and Al Azzam 2018:47; Zhao and Wen 2022:80-81; Shi 2007:197 also refers to corporate governance as a management framework whereby companies are controlled. Dbe 2003:269; Mongalo 2003:173.

⁴⁹ Shleifer et al 1997:737.

⁵⁰ Jabobs 2018:4.

⁵¹ Adams and Matheson 2000:1085.

investors.⁵² He further refers to the rule-based processes of laws, policies, and accountability that govern this relationship.⁵³ Dibra, Majmudar and Mongalo emphasized that corporate governance is concerned with managing corporations and separating corporate ownership from corporate control.⁵⁴

Similar to Dibra, Al Shunnaq and Al Azzam defined corporate governance as the rules, laws and standards that define the relationship between the company's management on the one hand and the shareholders and stakeholders on the other.⁵⁵ According to Dibra, Al Shunnaq, and Al Azzam, corporate governance is thus about the relationship between the company, the management of the company and shareholders and stakeholders and how to improve this relationship. They stressed that corporate governance is based on the relationship between management, shareholders and stakeholders; they did not examine possible causes of corporate collapse or preventative measures to prevent corporate failure.

Palmiter argued that corporate governance is a division of moral psychology. It is the product of moral values.⁵⁶ Rathbone and Kyereboah-Coleman hold that corporate governance is the rules and procedures utilised by the board of directors to ensure accountability by all stakeholders.⁵⁷ According to Horrington, in recognising the importance of corporate governance measures,⁵⁸ there has to be a balance between corporate governance measures, the interests of investors and the economic, environmental and social impact on society.⁵⁹ Corporate governance has been viewed as a survival mechanism by Adeyemi⁶⁰ and Mapitiya,⁶¹ and they concluded that corporate governance is a vital survival mechanism for a company to achieve its long-term goals to ensure ethical business and sustainable business practices in a competitive and turbulent economic

⁵² Dibra 2016:284; Cheffins 2012:22; Dbe 2003:269; Mongalo 2003:177.

⁵³ Dibra 2016:284; Cheffins 2012:22; Dbe 2003:269; Mongalo 2003:177.

⁵⁴ Dibra 2016:286; Majmudar 2021:74 emphasized that good corporate governance promotes fairness and safeguards an organisation's interests and prevents fraud. Mongalo 2003:174 noted that corporate governance is a process that include raising capital and managing those persons in control of the company.

⁵⁵ Al Shunnaq and Al Azzam 2018:47.

⁵⁶ Palmiter 2017:1120; Dbe 2003:269 noted that in order to improve corporate governance new codes of practice or amendments to existing laws and regulations may be effected.

⁵⁷ Rathbone 2020:181; Kyereboah-Coleman 2007:18.

⁵⁸ Transparency, financial liability, economic incentives, independent monitoring by the board of directors.

⁵⁹ Horrigan 2007:85

⁶⁰ Adeyemi 2019:32.

⁶¹ Mapitiya 2015:35.

environment. Cassim emphasised, similar to Adeyemi and Mapitiya, that a company's reputation, share price, and sustainability will likely be affected negatively should it fail to practice sound corporate governance.⁶²

Academic researchers Prasad,⁶³ Gillan and Stark⁶⁴ assert that corporate governance is an effective management system in the company's best interests. According to Goergen, corporate governance is a system for managing a company's stakeholders' interests.⁶⁵ Corporate governance is not merely compliance with legislation and various governance codes to ensure a stable economy. It is about the structures and processes created whereby a company is managed and controlled in the best interest of the stakeholders and other parties (external stakeholders, governments and local communities), cultivating an integrated culture of responsible behaviour and ensuring maximum efficiency.⁶⁶

Coglianese explains that procedural legitimacy is characterised by the separation of powers, transparency, and accountability.⁶⁷ These characteristics are parallel to corporate governance. Corporate governance refers to the separation of powers, transparency, integrated reporting, accountability, and board members' appointment and dismissal.⁶⁸ Substantive legitimacy is defined in terms of rights, such as rights enshrined in the Constitution.⁶⁹ The substantive legitimacy parallel is regulation imposed by the government.⁷⁰ Coglianese emphasized the substantive legitimacy of corporate governance, including the characteristics of corporate governance; however, methods to regulate and prevent corporate collapse were not emphasized.

Good corporate governance is essential because it raises business standards, encourages foreign investment, and enhances the performance of companies.⁷¹ Wiese argued that

⁶² Cassim et al 2018:271.

⁶³ Prasad 2014:3.

⁶⁴ Gillian and Stark 2000:275.

⁶⁵ Goergen et al 2010:469.

⁶⁶ Wiese 2018:2; Samaha et al 2012:168.

⁶⁷ Coglianese 2007:164.

⁶⁸ Coglianese 2007:162.

⁶⁹ For example, a fully functioning board cannot take decisions that would breach a constitutional right such as the right to freedom of expression or religion.

⁷⁰ For example, a fully functioning board cannot take decisions that would breach any law such as labour law or environmental law.

⁷¹ Anonymous 2003:269.

corporations do not operate in a vacuum and that the primary relationships between participants and corporations impact society, the environment, and the economy.⁷² Wiese, like Dibra, Al Shunnag, and Al Azzam, emphasised the relationship aspect of corporate governance rather than measures to prevent corporate failure. Majmudar emphasised corporate governance as a rules-based approach to administering a corporation without focusing on preventive measures to avoid corporate failure.⁷³ Neither Wiese nor Majmudar focuses on preventative measures. Corporate governance systems are essential for the growth of a country's economy and the recovery of public trust after a corporate collapse.⁷⁴ Transparent reporting, sound financial practices, and an accountable management and supervisory board are crucial components of a sound governance structure.⁷⁵ As defined by Toms,⁷⁶ A financial scandal can have a detrimental impact on innocent third parties and can enhance public demand for economic change and regulation that is both effective and efficient. The financial scandal involving Steinhoff had a detrimental impact on the company's shareholders, stakeholders, and public entities. Both Sundaram and Inkpen stressed the fact that practices of immoral corporate governance affect moral standards.⁷⁷

Zhao and Wen acknowledge the fact that board accountability should be understood as a social phenomenon in order to "*grapple with the full institutional complexity of corporate governance as a subject of legal enquiry.*"⁷⁸ According to Ogbodo and Umoru, the primary goal of corporate governance is to oversee the acts of management and directors and to mitigate the risks that emerge from the wrongdoing of corporate officers.⁷⁹ Majmudar referred to good corporate governance as a system that encourages fairness and openness to safeguard shareholders' rights and discourage fraud.⁸⁰ Thabane and Snyman Van Deventer⁸¹ concurred with the detailed definition of Du Plessis⁸² that corporate governance is the process of striking a balance between the competing interests of

⁷² Wiese 2018:2.

⁷³ Majmudar 2021:86-87; Mongalo 2003:175.

⁷⁴ Malgorzata et al 2018:87; Kyereboah-Coleman 2007:20.

⁷⁵ <https://www.theconversation.com/did-steinhoffs-board-structure-contribute-to-the-scandal> Accessed 28/01/2019.

⁷⁶ Toms 2009:478.

⁷⁷ Sundaram and Inkpen 2004:370.

⁷⁸ Zhao and Wen 2022:78.

⁷⁹ Ogbodo et al 2018:136. Majmudar 2021:74-76.

⁸⁰ Majmudar 2021:74. Mongalo 2003:173.

⁸¹ Thabane and Snyman Van Deventer 2018:3.

⁸² Du Plessis et al 2011:6-7; Majmudar 2021:73 states that corporate governance well governed corporations that are transparent will lead to investor confidence and raise capital effectively.

shareholders, internal stakeholders, and other parties who the actions of management may impact. This is done to ensure that the company operates at its highest possible level of productivity and profitability. According to Majmudar, good corporate governance entails maintaining healthy relationships over the long term and maintaining open lines of communication between investors and management.⁸³ Like Dibra Al Shunnag and Al Azzam, Majmudar focuses on the relationship framework between management and shareholders to ensure maximum profitability. Still, the connection between corporate governance and the prevention of corporate collapse was not shown.

Sheehy quoted Stephen Bottomley, who observed:

*"[c] corporate [g]overnance' is a slippery term: it is used both in discussions about the role of companies in society... and also in discussions about the organization of affairs within companies."*⁸⁴

Sheehy states that corporate governance asks and attempts to answer four questions, what is the entity being governed? By whom should the entity be governed? What is the best way to manage the entity, and in whose interests should the entity be governed?⁸⁵

According to Wiese, Al Shunnaq, and Al Azzam, the definition of corporate governance includes a management framework for regulating and supervising corporate conduct and balancing the interests of all stakeholders to ensure responsible corporate behaviour and maximise a company's efficiency and profitability.⁸⁶ According to Peng, the three significant factors of corporate governance are the shareholders, management and directors.⁸⁷ These factors are demonstrated in the Peng tripod below.⁸⁸ Peng's article, much like those of Dibra, Sheehy Wiese, Al Shunnaq, and Al Azzam, places its emphasis not on preventative measures but rather on the interaction that exists between management, shareholders, and stakeholders.

⁸³ Majmudar 2021:73.

⁸⁴ Bottomley 1997 as quoted by Sheehy 2005:194.

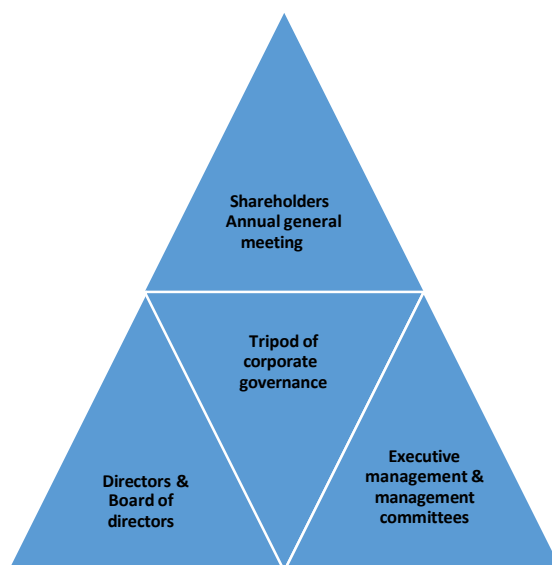
⁸⁵ Sheehy 2005:194.

⁸⁶ Wiese 2018:2; Al Shunnaq and Al Azzam 2018:47; Mongalo 2003:173.

⁸⁷ Peng 2008:323. The above figure was constructed by using the information obtained from Jacobs 2018:3.

⁸⁸ Jabobs 2018:3.

FIGURE 1 THE PENG TRIPOD OF CORPORATE GOVERNANCE



Based on the various definitions that have been presented, I believe that good corporate governance entails putting management systems in place to direct business operations and regulate the conduct of management to ensure responsible corporate behaviour, accountability, transparency, and fairness to all stakeholders and shareholders. I agree with Majmudar that this conclusion is based on the various definitions presented.⁸⁹ Improved corporate governance standards will ensure that the interests of shareholders, stakeholders and the company are balanced.⁹⁰

An important dimension of a sound governance structure is transparent reporting, sound financial practices and an engaged and accountable management and supervisory board; however, even though corporate governance standards and practices have been revised worldwide, as with Enron, accounting irregularities and significant financial losses remain undetected, as was the position in Steinhoff. Although much has been written on corporate governance's definition, preventing corporate collapse still needs to be settled. The general presumption is that corporate governance focuses on the relationship between management, directors, shareholders and stakeholders. Corporate governance's main

⁸⁹ Majmudar 2021:75.

⁹⁰ Mongalo 2010:3; Casado et al 2016:105; Mongalo 2003:177.

purpose is managing those controlling the corporation and raising capital in the interest of shareholders.

3. THEORIES, MODELS AND PERSPECTIVES OF CORPORATE GOVERNANCE

There are a multiplicity of different theories, models, perspectives, opinions, and definitions for corporate governance.⁹¹ However, Cremers warns

*"[c]orporate governance theories tend to defy easy classification, a recurring distinction is between the corporation as a social organization-largely based on notions of entity, centralization, and authority-and the corporation as a creature of the market-largely based on notions of individualism, decentralization, and contract."*⁹²

3.1 THEORIES

Both Otsuka⁹³ and Horrigan⁹⁴ assert that emerging theoretical perceptions must be assessed, and conventional corporate governance theories, models and measures must be challenged. Padfield states that various scholars have contributed to formalising three competing corporate governance models: director primacy, shareholder primacy, and team production. According to Padfield, all models attempt to try to identify.

*"(1) where the locus of control over the corporation does and/or should reside, and (2) toward what end that control is and/or should be exercised."*⁹⁵

⁹¹ Mupangavanhu 2016:18; Clarke 2005:343 states that for example in Japan a relationship-oriented system is followed. Wiese 2018:2; Clarke 2005:366.

⁹² Cremers et al 2016:736.

⁹³ Otsuka 2017:92.

⁹⁴ Horrigan 2007:86.

⁹⁵ Padfield 2015:6.

The different theories explained by Mupangavanhu⁹⁶ are the agency theory,⁹⁷ stewardship theory, stakeholder or concession theory,⁹⁸ and communitaire or shareholder theory.⁹⁹

3.1.1 AGENCY/CONTRACTURAL THEORY

Mapitiya¹⁰⁰ explains with reference to Tuan¹⁰¹ that most of the early definitions of corporate governance, also referred to as the narrow approach or agency theory, is that corporate governance is a system in which the interests of shareholders are paramount and must be protected against the potential abuse by directors.¹⁰² As observed by Moloi¹⁰³ and Alhumoudi,¹⁰⁴ the fundamental problem with this theory is the relationship between shareholders (the principals) and directors (the agents) in the event of directors who want to conduct the corporation's affairs in a self-serving manner.¹⁰⁵ An example is the Steinhoff collapse. In December 2017, shortly after Jooste (CEO) resigned, the Steinhoff board announced the appointment of PricewaterhouseCoopers to conduct an independent investigation into alleged accounting irregularities. The share price plunged by 60% resulting in a €10 billion loss in share value even though the board of the corporation is expected to safeguard the interests of the shareholders and ensure the overall success of the corporation.¹⁰⁶ Emery, Finnert and Stowe¹⁰⁷ noted that financial costs related to the

⁹⁶ Mupangavanhu 2016:42; Majamudar 2021:72-73.

⁹⁷ Agency theory also referred to as the shareholder centric theory or contractual theory views the interests of the stakeholders such as creditors, employees and environment as subordinate to the interests of shareholders. The theory emphasises the principles of freedom, competition and maximisation of profit. Majamudar 2021:78; Shi 2007:202; Zhao and Wen 2022:88.

⁹⁸ Concession theory views the company as a creature of state and the interest of stakeholders must be taken into account during the decision-making process. See Fort 1997 173-204 for a comprehensive discussion of the stakeholder theory and also Sheehy 2005:200-208.

⁹⁹ Communitaire theorists view the company as an instrument available to the state to expand the interests of a wider spectrum of stakeholders. Matheson and Olson 1992:1325-1329; Zhao and Wen 2022:83; Padfield 2015:11-13; Bisconti 2009:770; Adams and Matheson 2000:1094-1095; Cohen 1997:125. See also Sheehy 2005:209-225 for a full discussion of the shareholder theory.

¹⁰⁰ Mapitiya 2015:35; Zhao and Wen 2022:88 discussed the link between agency theory and board accountability and suggests that directors are regarded as agents of the stakeholders; therefore directors should be accountable to stakeholders.

¹⁰¹ Tuan 2014:46.

¹⁰² Mapitiya 2015:35; Majmudar 2021:75 argued that care must be taken to defend the self interest of shareholders above the strategic goals of the organization.

¹⁰³ Moloi 2008:17.

¹⁰⁴ Alhumoudi 2016:107; Azam 2011:2979.

¹⁰⁵ Thabane and Snyman Van Deventer 2018:7; Majmudar 2021: 75; Zhao and Wen 2022:88 noted that directors act as agents on behalf of shareholders and should be held accountable.

¹⁰⁶ Majmudar 2021:78 noted that if principals and managers fail to carry out the day-to-day objectives of the company it will lead to the financial failure of the company.<https://www.accountingweekly.com/why-steinhoffs-board-needs-to-be-held-accountable> Accessed 09-/03/2019.

¹⁰⁷ Emery et al 2004:376.

agency that occurred throughout the decision-making process could be significant, and an example hereof is the Steinhoff collapse, wherein the board of directors becomes the focal point of the governance system, being held responsible for successfully implementing a company's business plan and accountable to the shareholders.¹⁰⁸ The directors are regarded as agents of the company.¹⁰⁹

As illustrated by Tuan,¹¹⁰ the agency or contractual theory views corporate governance as a control system that includes laws, rules, and processes that control a company's operations to ensure economic freedom and focus on competition and maximising shareholder wealth.¹¹¹ The board of directors are the most critical component in the internal regulatory environment of the implementation of the governance code of an organisation.¹¹² The interests of stakeholders are seen as subordinate to those of shareholders.¹¹³ The challenges experienced with the agency theory are effectively being addressed by aligning the interests of owners and managers.¹¹⁴ In the Steinhoff collapse, the directors acted as the company's agents. The supervisory board and auditors had the financial and moral duties to serve in the best interests of the shareholders and stakeholders and failed dismally to discharge their duties. Earlier intervention by the risk and remuneration committees could have prevented exuberant bonuses paid to executives and could have mitigated losses.¹¹⁵

3.1.2 STEWARDSHIP THEORY

The stewardship theory views corporate governance from the legal perspective of the company that upon incorporation, the company becomes a separate legal entity from its shareholders.¹¹⁶ The shareholders appoint the directors whose duties are entrenched in

¹⁰⁸ IOD 2002. Majmudar 2021:76 referred to corporate governance as an effective apparatus to prevent abuse of administrative systems and ensure effective risk management.

¹⁰⁹ Mupangavanhu 2016:42; Majmudar 2021:76 emphasized that skilful, watchful and legit directors are essential for the profitability and effectiveness of an organization.

¹¹⁰ Tuan 2014:46.

¹¹¹ Mupangavanhu 2016:42. Majmudar 2021:74-76.

¹¹² Zhao and Wen 2022:80-81 noted that board accountability include internal responsibilities of the board towards the company and external legal obligations.

¹¹³ Moloi 2008:17.

¹¹⁴ Ntim et al 2012:85; Moloi 2008:25; Clarke 2005:36; Zhao and Wen 2022:88.

¹¹⁵ Crotty 2018: 1.

¹¹⁶ Thabane and Snyman Van Deventer 2018:8; Majamudar 2021:78 describes the stewardship theory as a social approach to human nature.

Section 76 of the Act to include fiduciary duties and the duty to exercise reasonable care, skill, and diligence that may reasonably be expected of a similarly situated and able person.¹¹⁷ The underpinning assumption is that directors are trusted to operate the organisation in the shareholders' interest, not their self-interest.¹¹⁸ According to Majmudar, the stewardship theory considers it the responsibility of management to ensure the organisation's success and not act as agents of the organisation.¹¹⁹

3.1.3 STAKEHOLDER/CONCESSION THEORY

One of the most cited books in management studies is *The Modern Corporation and Private Property* by Adolf Berle and Gardiner Means.¹²⁰ Berle and Means supported the stakeholder theory and promoted the philosophy of managerialism. Managerialism holds that the interests of a wide range of stakeholders, not just shareholders, should be considered during the decision-making process.¹²¹ The Berle-Means managerialism philosophy of corporate governance dominated American business from the 1930s to the 1970s.¹²² Johnson noted that since 1932

*"corporate law, or more narrowly corporate governance, has been preoccupied with the important problem of mending a potential rift between legal theory and reality: if shareholders are the chief beneficiaries of corporate activity-as legal orthodoxy holds-how does the law ensure that managers of publicly held corporations conscientiously operate those organizations to maximize shareholder wealth?"*¹²³

¹¹⁷ Thabane and Snyman Van Deventer 2018:10.

¹¹⁸ The stewardship theory rejects self-interest. Johnson 2019:1.

¹¹⁹ Majmudar 2021:78.

¹²⁰ Smith et al 2019:533-535; Cremers et al 2016:737; Johnson 1990:875; Matheson and Olson 1992:1330; Matheson and Olson 1994:1450; Padfield 2015:4; Pilon 1979:1255; Fort 1997:178; Fort 1998:248; Cohen 1997:131; Esser and Du Plessis 2007:347-348; Sheehy 2005:196.

¹²¹ Smith et al 2019:535; Zhao and Wen 2022:74; Cremers et al 2016:737; Matheson and Olson 1994:1450; Pilon 1979:1255.

¹²² The Berle-Means philosophy was not without controversy. Academics Lynn Stout and Professor Stephen Bainbridge rejected the idea of shareholder ownership and argued that shareholders own the residual claim on the company's assets and earning. Anand 2019:1521. Bainbridge 2002:22. Stout 2013:3; Licht 2004:652; Radin 2007:379.

¹²³ Johnson 1990:875.

Anand argues that in the Berle-Means model, the institutional shareholders' role is viewed as uninvolved in the decision-making process and disinterested in the management of the corporation.¹²⁴ Authors Smith¹²⁵ and Stout¹²⁶ have noted that the post-1980s rising levels of income inequality in the United States led to the displacement of Berle-Means managerialism philosophy by the reemerging shareholder value ideology. Loewenstein¹²⁷ states that

"The stakeholder movement, which began in the 1980s in the United States, was initiated by corporate directors seeking legislative protection for considering the interests of stakeholders other than shareholders when deciding how to respond to a hostile takeover offer."¹²⁸

Young and Thyl¹²⁹ state that an alternative to the agency or contractual theory is the stakeholder or concession theory, which was developed to focus on the pluralist interests of stakeholder groups, including customers, employees, creditors, suppliers, communities, and the environment.¹³⁰ This model is in sharp contrast to the contractual theory. The "bottom-up" concessionary theory argues that stakeholder interests must be considered during decision-making, benefitting the company in the short or long run.¹³¹

Cremers states that due to changes in corporate production and capital structures, companies need to promote investments from specific stakeholders, such as investments by employee groups, and develop long-term relationships with large customers and

¹²⁴ Anand 2019:1520; Majmudar 2021:76 noted that internal governance is determined by management, shareholders and debt holders. The board of directors are the most important component in the internal regulatory environment of the implementation of the governance code of an organization.

¹²⁵ Smith et al 2019:536.

¹²⁶ Stout 2012:1169.

¹²⁷ Loewenstein 2002:1673.

¹²⁸ Loewenstein 2002:1672-1673.

¹²⁹ Young et al 2009:168.

¹³⁰ Tuan 2014:52; Shi 2007:210; Licht 2004:651; see also Fort 1995:257-294 and Fort 1998:249-250; Cohen 1997:126.

¹³¹ Mupangavanhu 2016:44; Shi 2007:211.

creditors. All these stakeholders have become increasingly important in corporate profitability.¹³² They explain that transferring wealth from the shareholder to the stakeholder will ensure shareholder and firm value over the long term. The transfer should be to the shareholder's benefit.¹³³

3.1.4 COMMUNITAIRE THEORY

Communitarians emphasise the company's responsibility toward societal needs and the harmful effects between shareholder wealth pursuit and non-shareholder constituencies.¹³⁴ Similar to the contractarian theory, the directors are regarded as company agents. The ongoing discourse within South African law is around the communitaire, agency, and concession theories, as they pertain to determining the primary interests of shareholders.¹³⁵ There exists a divergence of opinions with respect to the dichotomy between shareholder primacy and stakeholder inclusivity. It has been asserted that South Africa has embraced the enlightened shareholder value approach under Act.¹³⁶ As per the findings of the King III report, a healthy and productive relationship with stakeholders must be maintained by directors to optimize long-term shareholder value.¹³⁷

Mupangavanhu posits that the theories pertaining to the essence of companies can be succinctly categorised into two prevailing models of corporate governance, namely the contractual or agency model, which emphasises a shareholder-centric perspective, and

¹³² Cremers et al 2016:793; Cohen 1997:126.

¹³³ Cremers et al 2016:794.

¹³⁴ Mupangavanhu 2016:42.

¹³⁵ Mupangavanhu 2016:43.

¹³⁶ Fisch and Solomon 2021:1311: "These arguments run counter to the traditional view that corporations should be managed with the primary goal of pursuing economic value for shareholders, often referred to as "shareholder primacy." Although commentators widely agree that shareholder primacy affords managers substantial latitude to consider the interests of non-shareholder constituencies a principle formalized in many areas of corporate law such as the business judgment rule, statutes authorizing corporations to donate money to charity, and, in many states, constituency statutes-the new discussion calls for corporations to shift their primary objective to incorporate a public purpose. Critics justify this shift by citing corporations' excessive focus on short-term profits, the negative externalities imposed by corporations on non-shareholder groups, and the need to address societal problems such as wealth inequality and climate change." Zhao and Wen 2022:83; Padfield 2015:11-13; Bisconti 2009:770; Adams and Matheson 2000:1094-1095; Cohen 1997:125.

¹³⁷ King III 2009:101.

the concession or stakeholder model, which considers the pluralistic interests of shareholders while also taking into consideration the interests of other stakeholders.¹³⁸

3.1.4.1 SHAREHOLDER-CENTRIC VIEW

The traditional shareholder primacy model is based on the principle that shareholders are the corporation's owners and are therefore entitled to control the company's destiny, determine its core policies, and may decide when to make fundamental changes in corporate policy and practice.¹³⁹

According to Cremers, proponents of the shareholder-centric model describe it as "*an efficient form of direct corporate democracy*,"¹⁴⁰ and they claim that the board-centric model is detrimental to the shareholders as board members "can unilaterally and opportunistically protect themselves from removal at the expense of shareholders."¹⁴¹ Cremers sees this as a very limited point of view because it fails to acknowledge the shareholders' limited commitment problem in some instances of prior shareholder consent.¹⁴² Cohen describes the shareholder model as a long-standing corporate law doctrine in which directors are responsible for making profits for the shareholders as residual owners.¹⁴³

The board ultimately remains responsible for successfully executing the company's business plan.¹⁴⁴ The board, directors, shareholders, and stakeholders are the most important corporate governance mechanisms.¹⁴⁵ The high levels of corporate governance provisions relating to corporate boards and directors have a stronger association with a firm value than disclosures related to other corporate governance provisions.¹⁴⁶ The

¹³⁸ Mupangavanhu 2016:44

¹³⁹ Matheson and Olson 1994:1461; Adams and Matheson 2000:1094-1095; Padfield 2015:11-13.

¹⁴⁰ Cremers et al 2016:734.

¹⁴¹ Cremers et al 2016:734.

¹⁴² Cremers et al 2016:734.

¹⁴³ Cohen 1997:125.

¹⁴⁴ Barac 2010:19.

¹⁴⁵ Ntim et al 2012:85.

¹⁴⁶ Ntim et al 2012:86.

assumption of shareholder primacy¹⁴⁷ has long been embedded in corporate law; however, the debate regarding whether stakeholders should have any formal role in corporate governance and whether their interests should be equal to those of shareholders is still ongoing.¹⁴⁸ Companies should act responsibly within the triple bottom line (economic, social, and environmental) and consider the triple bottom line factors when managing the company.¹⁴⁹ In contrast with two-tier systems, Japan applies a one-tier system with a flexible framework that synergies with communication accountability and control.¹⁵⁰

3.2 PERSPECTIVES

As Tricker demonstrates,¹⁵¹ there are different perspectives on the definition of corporate governance. These perspectives, as described by Tricker, can be from an operational perspective,¹⁵² a relationship perspective,¹⁵³ a stakeholder perspective,¹⁵⁴ a financial economics perspective,¹⁵⁵ a societal perspective,¹⁵⁶ and a shareholder perspective.¹⁵⁷

In recent years worldwide, corporate collapses and failures in banking institutions¹⁵⁸ prompted statutory intervention in the form of regulations to ensure that preventative measures are put in place and to facilitate the further development of sound corporate governance practices to improve fundamental issues of long-term sustainability, accountability, transparency, business ethics, and shareholder activism.¹⁵⁹ There will still

¹⁴⁷ Clarke 2005:345-347; Fisch and Solomon 2021:1311; Zhao and Wen 2022:83.

¹⁴⁸ Blount 2016:367.

¹⁴⁹ Cassim et al 2018:280.

¹⁵⁰ Clarke 2005:359.

¹⁵¹ Tricker 2012:4; Mongalo 2003:179.

¹⁵² The operational perspective places emphasis on the optimal practices pertaining to the interaction of the directors, management and shareholders. Tricker 2012:5; Mongalo 2003:180.

¹⁵³ A relationship perspective focuses on the mutual dependence amongst shareholders, management, employees, stakeholders and the environment. Tricker 2012:6; Shi 2007:210; Zhao and Wen 2022: 74-75.

¹⁵⁴ The stakeholder perspective has a broader outlook on individuals that are both involved and impacted than those included in the relationship perspective. Tricker 2012:7.

¹⁵⁵ The financial economics perspective places emphasis on the legal safeguards provided to investors and the allocation of capital ownership under corporate governance frameworks. Tricker 2012:7.

¹⁵⁶ A societal perspective attempts to include a broad spectrum of stakeholders who could be directly or indirectly affected by corporate behaviour.

¹⁵⁷ Cremers et al 2016:734.

¹⁵⁸ Royal Bank of Scotland, Société Générale. Wiese 2018:8; Riggins 2019:1.

¹⁵⁹ Cosama 2017:458; Fairfax 2008:18 noted that in Japan shareholder activism is on the increase because of the decrease number of investors attending annual general meetings.

be corporate failures due to the mismanagement of corporate risks, unimplemented or enforced regulations, poor corporate governance quality, or economic factors beyond the company's control.¹⁶⁰ New regulatory options have to be explored as it is clear that current corporate accountability practices are failing.¹⁶¹ As noted by Langeni:

*"[that] the most important requirements for effective corporate governance are developing an effective legal enforcement system, protecting stakeholders against exploitation of shareholders, transparency, and equal treatment of all shareholders."*¹⁶²

4. HISTORICAL BACKGROUND OF CORPORATE GOVERNANCE

Worldwide corporate scandals¹⁶³ and failures of high-profile companies had a widespread negative effect on shareholders, employees, consumers and communities.¹⁶⁴ Prisdani illustrates this statement with, for example, Reebok, Enron in 2001,¹⁶⁵ Satyam Computer Services, which in 2009 collapsed due to major company fraud,¹⁶⁶ and shortly after that, Global Crossing,¹⁶⁷ Xerox,¹⁶⁸ and WorldCom in America,¹⁶⁹ and Parmalat in Italy.¹⁷⁰ As

¹⁶⁰ Wiese 2018:179.

¹⁶¹ Sarre 2003:49.

¹⁶² Langeni 2018:49.

¹⁶³ <https://eujournal.org/index.php/esj/article/viewFile/7580/7307> Accessed on 17/02/2019.

¹⁶⁴ Sarra 2002:716.

¹⁶⁵ The company appeared to be well governed it had outside directors, an audit committee chaired by a chartered accountant, nomination and remunerations committees. Notwithstanding it was dysfunctional. Over the years directors formed special purpose entities and entered into complicated structured financial transactions which involved large amounts that were borrowed and kept off balance sheets. Bhasin 2013:25. Dbe 2003:271 noted that because of the Enron collapse corporate governance has become a major international concern and each country has its own unique corporate governance concerns. Sarra 2002:715 noted that the collapse of Enron was due to conflict of interest and failed oversight by directors. Stabile 2002:815; Ronen 2002:40; Owen 2003:169-170; Radin 2007:370; Dallas 2012:278.

¹⁶⁶ Bhasin 2013:25.

¹⁶⁷ The company had allegedly inflated earnings by using capacity swaps. Capacity swaps are the exchange of telecommunications capacity between carriers that is booked as revenue without money ever being exchanged. <https://www.theguardian.com/business/2002/jun/29/2> Accessed 13/4/2020. Stabile 2002:815; Owen 2003:171.

¹⁶⁸ In 2002 during the corporate scandal the company had overstated its revenues during the past five years. <https://www.thebalance.com/worldcom-s-magic-trick-356121> Accessed 13/4/2020. Emshwiller 2011:3.

¹⁶⁹ Dibra 2016:283; Sarra 2002:716; Ronen 2002:40; Emshwiller 2011:3; Owen 2003:170; Radin 2007:370.

¹⁷⁰ Parmalat was a typical example of strong managers and unprotected minority shareholders. Dibra 2016:282; Beechr-Monas 2007:379. See also Quinn 2014:58-59.

stated by Majmudar,¹⁷¹ several corporate scandals also made headlines in India, such as Reebok,¹⁷² Adidas, Kingfisher Airlines, Sahara, Kumar Mangalam Birla group, and Hero Motor Corporation.¹⁷³ In South Africa, collapses such as Saambou Bank,¹⁷⁴ Fidentia¹⁷⁵ and the 2017 Steinhoff collapse made the headlines. In Australia, the 1980s Bond Corporation and HIH group failures¹⁷⁶ Research and development of corporate governance ideas and practises continued in the 2000s.¹⁷⁷

As noted by Langeni, corporate governance remains relevant not only to the corporate sector but also to governments, academics, regulators, and society.¹⁷⁸ The economic crisis has also been referred to as a corporate governance crisis.¹⁷⁹ As emphasised by Mapitiya, the lack of sound corporate governance practices are considered a major cause of corporate collapses and economic crises.¹⁸⁰

In July 2002, the American Congress enacted the Sarbanes-Oxley Act of 2002 ("SOX")¹⁸¹ as a response to the corporate collapse of both Enron and WorldCom.¹⁸² To protect investors and change corporate governance, the SOX improved corporate transparency to prevent and identify corporate fraud, provide whistleblower legal protection, and expose fraudulent practises.¹⁸³ Reforms included in the SOX were restrictions on non-audit services that auditors could provide to audit clients and the formation of an independent Public Company Accounting oversight board.¹⁸⁴ Other reforms were the requirement that

¹⁷¹ Majmudar 2021:86-91.

¹⁷² Majmudar 2021:89.

¹⁷³ Majmudar 2021:91.

¹⁷⁴ Saambou Bank's collapse was as a result of poor management and liquidity problems <https://businesstech.co.za/news/banking/231009/all-the-south-african-banks-that-have-failed-in-the-past-30-years> Accessed 16/4/2020.

¹⁷⁵ As explained by Steenkamp 2007:40. Fidentia Asset Management failed to submit audited financial statements and funds were misappropriated. The roles of CEO and chairperson of the board were not separated. Directors did not act in the best interest of the company. The company did not act in good faith as clients' investments were used to defray business expenses.

¹⁷⁶ Allan 2006:139. The principal failure was the acceptance of the actuary's reports without it being tabled to the board or the internal audit department for evaluation nor was an actuary asked to attend the meeting to explain the report or answer questions. The board's inefficiencies included the CEO with unlimited authority, there was no independent non-executive director on the board and not a single independent director on the audit committee.

¹⁷⁷ Bekink 2008:95; Cassim et al 2018:271.

¹⁷⁸ Langeni 2018:18.

¹⁷⁹ Mupangavanhu 2016:1.

¹⁸⁰ Mapitiya 2015:32.

¹⁸¹ Johnson 2002:787; Sarra 2002:746.

¹⁸² Bhasin 2013:28; Dbe 2003:271; Stabile 2002:832; Emswiller 2011:3.

¹⁸³ Sarra 2002:747.

¹⁸⁴ Johnson 2002:787.

only independent directors form part of audit committees and compulsory off-balance-sheet transaction reporting, and increased penalties for corporate fraud were necessary.¹⁸⁵ Audit committees are essential in resolving financial reporting disagreements between auditors and management disagreements.¹⁸⁶ In 2004 following investigations into the state's public authorities' fiscal mismanagement and corruption, New York Governor George Pataki retained Ira Millstein as an advisor and chair of a committee on public authority and corporate governance.¹⁸⁷ The task was to develop and recommend solutions to ensure effectiveness and transparency in state entities.

As emphasised by Millstein, the explicit acknowledgement of aggressive reeducation and training and enforcement of fiduciary duties and better oversight should never be underestimated.¹⁸⁸ The commission drafted the Public Authorities Accountability Act of 2005, establishing an independent budget office to ensure transparency and responsible oversight.¹⁸⁹

The Cadbury Report,¹⁹⁰ the Greenbury Report¹⁹¹ and the Hampel Report¹⁹² in England, the Naresh Chandra Committee in India,¹⁹³ the Baums Report¹⁹⁴ and Cromme Code¹⁹⁵ in Germany¹⁹⁶ and the King Reports in South Africa are examples of comprehensive investigations of corporate governance.¹⁹⁷

¹⁸⁵ Martella et al 2004:62; Mongalo 2003:179.

¹⁸⁶ Martella et al 2004:65.

¹⁸⁷ Millstein 2017:163.

¹⁸⁸ Millstein 2017:169. Majmudar 2021:86.

¹⁸⁹ Millstein 2017:164.

¹⁹⁰ Cadbury Report dated 1992 on the financial aspects of corporate governance.

¹⁹¹ Chaired by Sir Richard Greenbury 1995 a report on director's remuneration. Mongalo 2003:175.

¹⁹² Mongalo 2003:175-177 noted that the Hampel committee placed significant emphasis on the notion that the board of directors bears the responsibility of enhancing shareholder investments and is held accountable to shareholders. The emphasis is on maximized shareholder return; this may be referred to as the narrow concept of corporate governance. Directors are accountable to only shareholders and no one else.

¹⁹³ Majmudar 2021:79 The committee was tasked to investigate two areas of corporate governance, financial and non-financial disclosures, board supervision of management and independent audits. The committee was tasked to create a framework for ethics, best practices, raising the standard of corporate governance in India. To foster a culture of voluntary, compliance and facilitate effective participation of various stakeholders in promoting good corporate governance.

¹⁹⁴ As noted by Majmudar 2021:88 the Baums report was released in 2001 recommended changes to German legislation to attract investors.

¹⁹⁵ As described by Majmudar 2021:86 the Cromme Code established regulatory measures for improved transparency and oversight.

¹⁹⁶ Majmudar 2021:88.

¹⁹⁷ Bekink 2008:107. Majmudar 2021:79 The tasks of the Committee in India was similar to the tasks of the King Committee.

4.1 CADBURY REPORT

The Cadbury Committee (the "committee") was established in 1992 by the Financial Reporting Council, the London Stock Exchange, and the accounting profession.¹⁹⁸ The main reason was to take action given the increased realisation that there was a decline in the international business competitiveness of the United Kingdom.¹⁹⁹ The intent of Cadbury²⁰⁰ and the committee was to improve corporate governance standards and confidence in financial reporting and auditing following numerous unexpected corporate failures and scandals.²⁰¹ The draught report was made available for public comment on May 27, 1992, and the final report was officially dated December 1, 1992.²⁰² According to the Cadbury report, corporate governance is the established framework through which companies are managed and governed.²⁰³ The fundamental objective of corporate governance is to ensure the efficient and effective discharge of responsibilities by a board of directors within the context of a robust framework of good corporate governance.²⁰⁴ The primary responsibility for the corporate governance of public corporations is with the board of directors.²⁰⁵

The Cadbury committee provided significant recommendations pertaining to the financial dimensions of corporate governance.²⁰⁶ The study has been recognised as a landmark contribution to the field of corporate governance. The approach is oriented towards practical application and is strengthened by the implementation of the Code of best practise, which includes inherent mechanisms for verification and accountability.²⁰⁷ The committee noted that no corporate governance system could be absolute proof against fraud or incompetence.²⁰⁸

¹⁹⁸ Du Plessis 1994:81; Mongalo 2003:173.

¹⁹⁹ Du Plessis 1994:81.

²⁰⁰ Visser et al 2010:97.

²⁰¹ The Maxwell and BCCI scandals. Majmudar 2021:87.

²⁰² Du Plessis 1994:81.

²⁰³ Cadbury report 1992:15; Jungmann 2006:428.

²⁰⁴ Cadbury report 1992:5; Mongalo 2003:175.

²⁰⁵ Langeni 2018 :19; Mongalo 2003:175-191.

²⁰⁶ Du Plessis 1994:89; Mongalo 2003:175-176.

²⁰⁷ Majmudar 2021:87; Mongalo 2003:175.

²⁰⁸ Cadbury report 1992:53.

The critical safeguards include division of responsibilities between the chairman and chief executive officer functions, appropriately structured boards, audit committees, diligent shareholders, and financial reporting and audit mechanisms that provide comprehensive and timely disclosure.²⁰⁹The committee proposed a Code of best practise, referred to as "The Code," that outlines overarching principles aimed at enhancing corporate governance standards.²¹⁰ The committee made various recommendations on specific aspects: the composition of the board of directors and a prominent role of non-executive directors, the establishment of auditing committees and free control of auditors, the role of the company's shareholders, and transparency and improved control over executive remuneration.²¹¹

4.1.1 BOARD OF DIRECTORS

The Cadbury committee recommended the establishment of a proficient board of directors to assume leadership and governance responsibilities within the company.²¹² The board is comprised of both executive directors, who possess extensive knowledge of the company, and non-executive directors from external sources. This composition allows for a comprehensive perspective on the company's activities. The chairperson assumes the duties and responsibilities associated with the position.²¹³ The board appoints appropriate executive and non-executive directors.²¹⁴ It is recommended that the roles of chairperson and chief executive officer be held by separate individuals. The responsibilities of the board encompass the establishment of strategic objectives, the provision of leadership in their implementation, the oversight of corporate management, and the communication of their stewardship to shareholders.. The meaning of board management was described by the Appeal Court in *Lipschitz and Another v Wolpert and Abrahams*:

"[as] the general body of shareholders put up and risk their money (to extent of their shares), yet they have no control over or knowledge of the day-to-day administration of a company."²¹⁵

²⁰⁹ Du Plessis 1994:90.

²¹⁰ Du Plessis 1994:82.

²¹¹ Majmudar 2021:86-87.

²¹² Wiese 2018:29.

²¹³ Cadbury report 1992:15.

²¹⁴ Cadbury report 1992:19.

²¹⁵ *Lipschitz and Another v Wolpert and Abrahams* 1977 (2) SA 732 (A) see Lee 2005:68.

Regarding current corporate law, boards have two primary functions: monitoring and management.²¹⁶

The chairperson's functions are to ensure that the agenda contains all relevant issues and is received timeously by the non-executive directors.²¹⁷ The primary function of the non-executive director is to oversee and evaluate the performance of the board of directors and the chief executive officer. An evaluation of the board's efficacy includes the collaborative dynamics among board members under the guidance of the chairperson, as well as their capacity to offer leadership and impartially examine the company's governance procedures.²¹⁸ The committee made a recommendation to appoint various committees within the board.²¹⁹

4.1.2 NON-EXECUTIVE DIRECTOR

The Cadbury committee acknowledges that most non-executive directors should be independent of management and make impartial judgements on standards of conduct, important appointments, strategy, resources, and performance.²²⁰

The committee notes that the responsibility for appointing non-executive directors ought to reside with the board, and emphasises that their appointment on specific conditions and subsequent reappointment should not be carried out automatically.²²¹

4.1.3. AUDIT COMMITTEE

The Cadbury committee considers auditing an integral part of corporate governance. It makes valuable suggestions to develop internal control methods and increase the audit's effectiveness and value.²²² These proposals include narrowing the expectation gap (the

²¹⁶ Matheson and Olson 1994:1446.

²¹⁷ Cadbury report 1992:20; Lee 2005:67-69.

²¹⁸ Cassim et al 2018:279.

²¹⁹ Audit remuneration and nomination committees.

²²⁰ Cadbury report 1992:58.

²²¹ Cadbury report 1992:59.

²²² Cassim et al 2018:278; Martella et al 2004:65.

difference between what audits achieve and what it is expected to achieve or should achieve), developing a set of criteria for assessing the effectiveness, and developing guidance for companies on the reporting format of directors and auditor concerning to fraud and other illegal acts, the committee submits that it is primarily the board's responsibility as part of its fiduciary responsibility to protect the company's assets and monitor statutory compliance.²²³

The independent audit committee is responsible for supervising the audit process. The provision of an independent and objective assessment on the credibility of directors' financial statements, which serve as the foundation of the reporting system, offers shareholders a valuable instrument.²²⁴ The independent audit committee is responsible for supervising the audit process. The provision of an external and objective check on the integrity of directors' financial statements, which serve as the foundation of the reporting system, offers shareholders a valuable safeguard.²²⁵

Referring to the issue of auditors' liability, the committee's discussion revolves around the decision in *Caparo Industries Plc v Dickman, Dickman, and Touche Ross*.²²⁶ The decision arose in the context of a negligent preparation of accounts for a company. The House of Lords had to carefully balance the complex interests of auditors and shareholders who suffer losses due to professional negligence and the public interest in having a viable and fair system.²²⁷ The House of Lords concluded that auditors have a legal obligation to exercise due care towards the company and its shareholders collectively. However, this responsibility does not extend to individual shareholders or external parties who depend on the audited financial statements for the purpose of purchasing shares in the company.²²⁸ The case has caused controversy because it exposed two widely held misconceptions that the audit report guarantees the company's soundness and that anyone can rely on the audit and sue the auditors if they are negligent.²²⁹

²²³ Cadbury report 1992:43.

²²⁴ Cadbury report 1992:15.

²²⁵ Cadbury report 1992:28.

²²⁶ *Caparo Industries Plc v Dickman, Dickman and Touche Ross & Co* (1990) 2 WLR: 358 (HL).

²²⁷ Du Plessis 1994:88; Mongalo 2003:174.

²²⁸ Cadbury report 1992:45.

²²⁹ Cadbury report 1992:45.

In the final report, the committee concluded that there needs to be a consensus on a satisfactory way of reconciling the conflicting interests of auditors and investors and that the committee will monitor further developments.²³⁰

4.1.4 SHAREHOLDERS

The Cadbury committee addresses the apprehensions of shareholders that arise predominantly from the distinction between ownership and control within public companies..²³¹ The committee provides commentary on strengthening the accountability of boards of directors towards shareholders in the context of corporate governance.²³² Proposals pertaining to this matter were presented by individual shareholders as well as shareholder organisations.²³³ One was the formation of shareholder committees to ensure close involvement in the appointment of directors and auditors. The other suggestion was to simplify how resolutions were put forward at general meetings. The committee did not recommend the establishment of compulsory shareholder committees because there was no evidence at the time explaining how shareholder committees can become an efficient link between a board and the shareholders.²³⁴

4.1.5 EMPLOYEE PARTICIPATION ON THE BOARD

The Cadbury committee did not propose the inclusion of employee participation on the boards of public corporations.²³⁵

5. THE CODE OF BEST PRACTICE

The primary objective of the Code is to enhance the standard²³⁶ of corporate governance and promote mechanisms for oversight and accountability within the corporate

²³⁰ Cadbury report 1992:46.

²³¹ Du Plessis 1994:86 Mongalo 2003:179.

²³² Cadbury report 1992:48.

²³³ Du Plessis 1994:86.

²³⁴ Cadbury report 1992:48.

²³⁵ Du Plessis 1994:87; see also Clarke 2005:339-370 on worker's participation on management boards in Japan.

²³⁶ Visser et al 2010:97.

framework.²³⁷ The Code applies to all listed companies and is published separately from the final report. The Code has three elements: leadership, sustainability, and good corporate citizenship. It is based on openness, integrity, and accountability.²³⁸ It refers to financial reporting and aspects concerning all listed companies' boards of directors, executive directors, and non-executive directors of all listed companies.²³⁹ The Code requires a clear separation of duties within a corporation and a balance of power and authority at its highest levels to ensure that nobody has unlimited decision-making power.²⁴⁰ The committee submitted that some corporate failures and scandals could have been prevented had a code of best practices existed.²⁴¹ The Code contains multiple built-in checks and balances, enhancing the report's practical usefulness.²⁴² The role of implementing the Code in Steinhoff's failure is also partly due to the lack of proper implementation of corporate governance practices and ensuring the adherence to established standards of behaviour and not just another tick-box exercise for compliance's sake. Improving the standards of corporate governance by structures and rules alone cannot be achieved.²⁴³

6. CORPORATE GOVERNANCE MECHANISMS

6.1 INTRODUCTION

Horrigan²⁴⁴ and Shi²⁴⁵ submit that multiple legal and regulatory mechanisms and measures exist to enhance corporate governance and prevent corporate failure. These mechanisms include arranging corporate meetings and engaging with shareholders and stakeholders to develop corporate decision-making frameworks and guidelines, comply with corporate codes of conduct, and adhere to and implement corporate governance principles.²⁴⁶ Shi and Horrigan explored the mechanisms and measures to enhance corporate governance

²³⁷ Du Plessis 1994:83.

²³⁸ Cadbury report 1992:16.

²³⁹ Du Plessis 1994:83; Cadbury report 1992:16.

²⁴⁰ Du Plessis 1994:83; Mongalo 2003:173.

²⁴¹ Du Plessis 1994:82; Mongalo 2003:173-178.

²⁴² Du Plessis 1994:89.

²⁴³ Cadbury report 1992:18.

²⁴⁴ Horrigan 2007:99.

²⁴⁵ Shi 2007:197.

²⁴⁶ Shi 2007:197-198; Prisdani 2020:22.

without referring to measures and systems to prevent corporate collapse. According to Cunningham, corporate governance mechanisms can be categorised into three distinct groups, namely internal-horizontal and external methods.²⁴⁷ Cunningham asserts that the internal governance mechanisms implemented by the corporation can be classified as vertical when they apply to the management of the interaction between the individuals in control of the company and other shareholders and stakeholders.²⁴⁸ The internal-horizontal processes govern the interrelationships between the different stakeholders, including the corporation's bylaws.²⁴⁹ External governance mechanisms are the rules and regulations applicable to the corporation outside the internal management and operations of the company²⁵⁰ The primary responsibilities of an organization's management are establishing strategic direction, approving policies and planning, overseeing and monitoring the organization's activities, and ensuring accountability.²⁵¹

The King IV report contains 17 principles to guide organisations when implementing corporate governance practises, with the ultimate aim of establishing effective and ethical corporate governance.²⁵² In Chapter 5, the corporate governance practises of Steinhoff will be assessed through the use of these 17 principles

Leadership, ethics and corporate citizenship

Principle 1: Ethical and effective leadership by the governing body

Principle 2: The governing board ought to exercise oversight over the ethical standards of the organisation in a manner that promotes the cultivation of an ethical culture.

Principle 3: Responsible corporate citizenship

²⁴⁷ Cunningham 1999:1134.

²⁴⁸ Cunningham 1999:1134.

²⁴⁹ Cunningham 1999:1134; Jones 2006:883; see Bruner 2011: "*Though an ostensibly mundane and mechanical instrument of corporate governance, the bylaws lend themselves to such efforts because - perhaps surprisingly - enacting, amending, and repealing bylaws are essentially the only corporate governance actions that shareholders can undertake unilaterally.*"

²⁵⁰ Cunningham 1999:1134.

²⁵¹ King IV 2016:40.

²⁵² King IV 2016:40-41; <https://clearlawsa.org.za/wp-content/uploads/2021/03/THE-17-PRINCIPLES-OF-KING-IV-ON-CORPORATE-GOVERNANCE.pdf> Accessed 25/04/2023.

Strategy, performance and reporting

Principle 4: The executive team should recognise that the corporation's fundamental mission, associated risks, strategic approach, performance, and sustainable development are all interconnected components of the process of value creation.

Principle 5: The governing body needs to ensure that the corporation's reports allow stakeholders to evaluate its performance and short-, medium-, and long-term prospects.

Governing structures and delegation

Principle 6: Board as custodian of good governance

Principle 7: Board composition

Principle 8: Effective board structures and delegation of authority

Principle 9: Board performance evaluation

Principle 10: Board/management relationships

Governance functional areas

Principle 11: Risk governance

Principle 12: Technology and information governance

Principle 13: Compliance governance

Principle 14: Remuneration governance

Principle 15: Assurance

Stakeholder relationships

Principle 16: Stakeholder-inclusive approach

Principle 17: Responsible investment

6.2 INTERNAL CORPORATE GOVERNANCE MECHANISMS

Internal corporate governance mechanisms govern the relationship between the board, managers, shareholders and stakeholders. The primary governance role and responsibilities of the board and managers are to set the strategic direction, approve policies, oversee and monitor management and ensure accountability. The board structure and composition play an essential role in corporate governance. Countries' board structures differ due to political, cultural and social backgrounds.²⁵³

6.2.1 BOARD COMPOSITION

As explained by Shi,²⁵⁴ the board composition refers to the number of executive and non-executive directors²⁵⁵ and the number of independent and affiliated directors and shareholder-elected and employee-elected directors. According to Shi,²⁵⁶ 'independence' also includes non-executive directors who do not have a contractual relationship with the company, not associated directly (as a consultant) or indirectly with the company as a material supplier or customer. An independent director includes someone who hasn't been appointed as a principal or material professional advisor within the last few years associated with a service being provided to the company.²⁵⁷

Brudney²⁵⁸ describe "independence" as:

"In the narrowest terms, independence refers to the relationship of the directors, as representatives of stockholders, to management. The independent director is expected to be selected by stockholders alone and to oversee management in their interests. Broader conceptions of independence contemplate directors who are not merely independent monitors of management on behalf of stockholders, but who have loyalties to specific constituencies, such as labor, consumers, women, minorities, or the public affected by environmental and other consequences of corporate activity." 259

²⁵³ Shi 2007:197-212 compared the different board structures and board compositions of Australia and Germany.

²⁵⁴ Shi 2007:197.

²⁵⁵ Non-executive directors are not involved in the day-to-day management of the company and are not full-time employees of the company. Shi 2007:197-200.

²⁵⁶ Shi 2007:200-201.

²⁵⁷ Shi 2007:201.

²⁵⁸ Brudney 1982:599.

²⁵⁹ Brudney 1982:599.

Samol explained that the hybrid board structure in Japan, which includes a convergence between one- and two-tier board systems, can address the needs of most types of international companies, especially taking into account access to information and balance of power within the company the hybrid board system in Japan is the most progressive approach to company board hybridization.²⁶⁰

6.2.2 ONE-TIERED SYSTEM

One-tiered board systems are widespread internationally and comprise a single management body and are adopted by Ireland, Sweden, Turkey, Switzerland, Switzerland and Korea.²⁶¹ In practice, the dual board system was also established in other continental European. Intensive interaction occurs between the management board and the supervisory board.

6.2.3 TWO-TIERED SYSTEM

The two-tiered system is also referred to as a dual-board system. It is a widespread management system in continental Europe,²⁶² such as Germany, Sweden, the Netherlands,²⁶³ Poland,²⁶⁴ Finland, and Denmark.²⁶⁵ It is also known as the "double board" or "dual-tier board" system as opposed to the single executive board of directors in most English companies.²⁶⁶ The two-tiered board system comprises two separate boards that function together.²⁶⁷ The supervisory board represents the employees and shareholders, and the management board includes the companies' executives.²⁶⁸

6.3 EXTERNAL CORPORATE GOVERNANCE MECHANISMS

²⁶⁰ Samol 2016:216.

²⁶¹ Prisdani 2019:26; Shi 2007:204.

²⁶² Shi 2007:204; Harnos 2015:93; Fanto 1998:116 explains that "*French companies can adopt a two-tiered board, which is already permitted under French corporate law, or have a unitary board structure.*"

²⁶³ Beecher-Monas 2007:379; Jungmann 2006:426.

²⁶⁴ Samol 2016:67.

²⁶⁵ Jungmann 2006:426.

²⁶⁶ Moss 2020:74; Moloney and Murphy 2013:141.

²⁶⁷ Fairfax 2008:13 noted countries where the two-tiered system is the norm include Czech Republic, Germany, Poland and Russia; Prisdani 2020:26.

²⁶⁸ Majmudar 2021:87; Shi 2007:197-212; Walter 1988:653.

External governance mechanisms are the rules and regulations applicable to the corporation outside the internal management and business of the corporation and the direct interests of the corporation, such as competition and antitrust laws, rules and policies on national trade, and public health and safety.²⁶⁹

7. CHALLENGES EMANATING FROM THE APPLICATION OF SOUND CORPORATE GOVERNANCE MECHANISMS

Sound corporate governance practices and mechanisms are essential for the economic development of a country. Poor corporate governance will negatively influence a corporation's share price, and poor sustainability will negatively influence the share price, sustainability and reputation.²⁷⁰ I am of the opinion that corporate governance is a set of principles and recommended practices that guide the top management of corporations to ensure accountability, transparency, and fairness. The Steinhoff collapse is the perfect example of how management's failure to implement the corporate governance mechanisms correctly resulted in Steinhoff's collapse. While the suggested mechanisms are intended to promote sound management and prevent corporate scandals, several challenges can hinder their effectiveness. Some of the common difficulties with the application of corporate governance practices are:

Lack of support and commitment from management: Corporate governance practices require the support and commitment of management to be effective. However, challenges may arise if some leaders may not fully comprehend the importance of corporate governance or the application thereof. This may result in prioritising short-term financial goals over long-term sustainability and ethical considerations.

Shareholders play a critical role in corporate governance by holding corporations accountable for their actions²⁷¹. However, if shareholders are not actively involved or informed about their rights and responsibilities, it can limit their ability to influence company

²⁶⁹ Cunningham 1999:1134.

²⁷⁰ Cassim et al 2018:271.

²⁷¹ Da Silva 2019:36. <https://www.moneyweb.co.za/news/companies-and-deals/lots-of-no-votes-at-steinhoff-agm/> Accessed 05/05/2021.

decisions and hold management accountable for their actions. Low levels of attendance by shareholders were observed at Steinhoff's annual general meetings.²⁷² The shareholders had the opportunity to interrogate the financial statements and decisions made by management and vote on significant matters.

I believe that the complexity of corporate structures and weak regulatory frameworks ultimately resulted in the Steinhoff management failing to have sufficient oversight to ensure transparent and accurate reporting.

Continuously reviewing corporate governance measures and practices may require significant changes to a company's top management, culture, processes, and decision-making structures. Ongoing efforts to strengthen corporate governance practices may create resistance from employees and managers who are comfortable with the status quo or fear losing power or influence. The collapse of Steinhoff is the result of failed corporate governance measures and practices. It significantly impacted various shareholders and stakeholders, including employees, pension funds, suppliers and customers. Financial markets and shareholders suffered substantial financial losses when share prices plummeted by more than 95% within the first week after Jooste resigned. Investors lost confidence in the accounting and auditing processes of Steinhoff. Steinhoff employees suffered job losses worldwide, and the company's collapse severely impacted their livelihoods. Others had their pensions and retirement savings tied up in Steinhoff shares and lost a significant portion of their savings. Many Steinhoff investors lost a substantial amount of their savings. Suppliers were negatively impacted by the collapse of Steinhoff and had to write off debts which impacted their profitability and cash flow. Overall, the collapse of Steinhoff had a significant impact on a wide range of stakeholders, and its effects are likely to be felt for many years to come.

8. CONCLUSION

²⁷² <https://www.moneyweb.co.za/news/companies-and-deals/lots-of-no-votes-at-steinhoff-agm/> Accessed 03/05/2021.

This chapter has laid down the historical and theoretical foundations for focusing on the fundamental concepts of corporate governance central to this thesis. It has explained the limits of corporate governance.

This chapter focused on corporate governance's origin, sources, and basis, the nature and forms of corporate collapse, and the prevention thereof. It adopted a historical approach wherein the Cadbury report's committee proposals were discussed. The committee proposed a Code of Best Practice that sets out the general principles designed to raise the standards of corporate governance.²⁷³ The committee made recommendations regarding the composition of the board of directors, the formation of auditing committees, the role of the company's shareholders, and the responsibilities of the non-executive director.²⁷⁴

The chapter indicated the various role players responsible for corporate governance in a company.²⁷⁵ It explained the application of enhanced transparency per Chapter 3 of the South African Companies Act²⁷⁶ ("the Act"), King I, II, III, and IV report.

The theoretical framework of corporate governance was explored. The chapter examined the agency, stakeholder, and communitaire theories. I believe that based on the literature reviewed, the agency theory is more important than either the stakeholder or communitaire theories as it has more bearing on the application of corporate governance on the one hand and the effect thereof on the other.

Importantly, this chapter defined corporate governance and its nature. I believe the board's role in Steinhoff's collapse is also partly due to the lack of independence and oversight. The board is in charge of the sustainable leadership of the company, and corporate governance serves as an objective instrument used to measure the standard of practices of those governing a company. It reminds boards and managers that they will be day-to-day accountable for their daily decisions. Directors and senior

²⁷³ Du Plessis 1994:82.

²⁷⁴ Du Plessis 1994:83-84.

²⁷⁵ Lee 2005:68.

²⁷⁶ 71 of 2008.

managers could personally be held responsible in the event of corporate governance failure. Without implementing robust corporate governance practices and processes, risk management processes will be ineffective, and the company's strategic plan will be based on incorrect data, resulting in the board making decisions based on erroneous data. The company could be faced with reputational damages and sanctions for non-compliance.²⁷⁷

In general, I am of the opinion that the disastrous effect of a failure in corporate governance, such as the collapse of Steinhoff, demonstrates the necessity for continual efforts to develop corporate governance practices and foster a culture of transparency, accountability, and ethical behaviour.

²⁷⁷ <https://www.diligent.com/insights/entity-governance/modern-governance-corporate-governance-changing/> Accessed 22/10/2022.

CHAPTER 3: TIMELINE OF THE CORPORATE COLLAPSE OF STEINHOFF

1. INTRODUCTION

In this chapter, the business and management structures of Steinhoff as well as the timeline of the collapse of Steinhoff, will be set out. The chapter aims to give an overview of Steinhoff and the timeline to serve as background for the chapters to follow. Newspaper reports are used as their coverage of the Steinhoff collapse as it unfolded gives the timeframe.²⁷⁸

The Steinhoff scandal²⁷⁹ started on 5 December 2017 when the Steinhoff CEO, Markus Jooste, resigned. The Steinhoff board announced the appointment of PricewaterhouseCoopers Advisory Service Proprietary Limited (PwC) to conduct an independent investigation into the occurrence of alleged potential accounting irregularities or potential non-compliance with laws and regulations impacting Steinhoff's financial statements.²⁸⁰ These alleged irregularities are related to fictitious transactions, off-balance sheet items and possible misrepresentations of earnings.²⁸¹

Steinhoff International Holdings N.V. ("SIHNV") is an integrated, multinational retailer with 2000 globally registered subsidiaries.²⁸² As a multinational company, it manufactures and retails furniture and household groups in Europe, Africa and the Pacific Rim and deals in more than 40 different jurisdictions,²⁸³ which includes the JD Group and Pepcor in South Africa.²⁸⁴ With over 40 retailing brands²⁸⁵ in over 30 countries, Steinhoff was positioned as one of the largest companies by market capitalisation on the JSE exchange.²⁸⁶ In 2017 it

²⁷⁸ Newspaper reports are used as their coverage of the Steinhoff collapse as it unfolded, gives the timeframe. <https://www.cnbcfrica.com/2019/pwc-steinhoff-report-out> Accessed 09/03/2019.

²⁷⁹ <https://mg.co.za/article/2018-04-09-steinhoffs-board-behaved-badly-why-it-needs-to-be-held-to-account> Accessed 09/03/2019.

²⁸⁰ <https://www.cnbcfrica.com/2019/pwc-steinhoff-report-out/> Accessed 14/04/2019.

²⁸¹ <https://in.reuters.com/article/us-steinhoff-intln-accounts/pwc-investigation-finds-74-billion-accounting-fraud-at-steinhoff-company-says-idINKCN1QW2C2> Accessed 02/10/2020.

²⁸² Styan 2018:57.

²⁸³ <https://www.companiesthistory.com/steinhoff-international/> Accessed 17/10/2020.

²⁸⁴ Styan 2018:59.

²⁸⁵ <http://www.steinhoffinternational.com> Accessed 7/3/2019.

²⁸⁶ <https://www.news24.com/fin24/companies/retail/steinhoff-on-brink-of-dropping-off-jses-top-100-company-list-20171221> Accessed 02/10/2020.

was placed in the top 10 companies, flanked by media giant Naspers, Richemont, Anglo-American, Sasol, Standard Bank and Firstrand.²⁸⁷

2. TIMELINE OF THE STEINHOFF BUSINESS AND COLLAPSE

The founder of the multinational company, which procured low-cost furniture from East Germany and sold it to West Germany, was Bruno Steinhoff.²⁸⁸ During the early 1990s, the paths of Steinhoff and Jooste would cross. In 1998 Steinhoff Europe and Steinhoff Africa (formerly Gommagomma) consolidated their business operations. Each focused on establishing a low-cost furniture manufacturing and supply base Steinhoff Africa focused on developing an integrated furniture and household goods business.²⁸⁹

As described by Cronje,²⁹⁰ "Steinhoff International Holdings" (corporate seat in Amsterdam in the Netherlands) became the umbrella parent firm of Steinhoff Europe and Steinhoff Africa. The headquarters of Steinhoff is in South Africa, and since 2015 is primarily listed on the Frankfurt Stock Exchange in Germany.²⁹¹

Steinhoff entered on three fronts: the UK, African and Australian markets, established sourcing operations in Asia, and made inroads into the raw supply material fields. In 1999 JSE announced the acquired factories from Klose Group Braecroft Timbers, Megacor Holdings, and Cornick Group (including the Afcol assets)²⁹² and took over the management of Panda Sofa (Australia).

2000: the acquisition of the Klose Collection in Germany gave Steinhoff access to three high-tech factories and Klose Hungary. Steinhoff also expanded its footprint in Poland by acquiring five Polish upholstery factories, including Prudnik.²⁹³

²⁸⁷ <https://www.moneyweb.co.za/news/companies-and-deals/steinhoff-saga-points-to-major-corporate-behaviour-gaps> Accessed 8/3/2019.

²⁸⁸ Cronje 2017:5.

²⁸⁹ Naude et al 2018:7.

²⁹⁰ <https://www.news24.com/fin24/Companies/Retail/a-steinhoff-guide-for-dummies-20172018> Accessed 08/11/2020.

²⁹¹ <https://www.news24.com/fin24/Companies/Retail/a-steinhoff-guide-for-dummies-20172018> Accessed 08/11/2020.

²⁹² https://www.sharenet.co.za/free/sens/disp_news.phtml? Accessed 10/11/2020.

²⁹³ Steinhoff annual report 2004:15.

2001: Acquired Relyon Group (UK) and Steinhoff Pacific are formed²⁹⁴ and acquired Marshall Furniture (Australia) and the Freedom Group (Australia and New Zealand). Acquired Dieterknoll and Egofurn brand and formate a La-Z-Boy joint venture for Europe.²⁹⁵

2002: Acquired Dieter Knoll. Entered into a joint venture with La-Z-Boy (in the US). Acquired an interest in PG Bison Holdings and increased its stake in Unitrans.²⁹⁶

2003: Acquired Sprung Slumber (UK) an interest in Puris Bad GmbH. Privatised and publicly listed the Freedom Group.²⁹⁷

2004: Acquired the remaining interest in PG Bison, the assets of Hukla Möbelwerke.²⁹⁸

2007: Acquired the remaining minority interest in Homestyle and Unitrans Limited and was delisted from the London Stock Exchange.²⁹⁹

2008: The founder, Bruno Steinhoff, retires and becomes a non-executive director.³⁰⁰

2009: 19 000 permanent South African employees and managers become shareholders in Steinhoff due to a Broad-based black economic empowerment transaction.³⁰¹

2010: Acquired the remaining interest in Hemisphere International Properties BV.

2011: Acquired Conforama Holdings.³⁰²

2012: Acquired a controlling interest in JD group.³⁰³

²⁹⁴ Steinhoff annual report 2004:15.

²⁹⁵ Cronje 2017:4.

²⁹⁶ Steinhoff annual report 2004:16.

²⁹⁷ Steinhoff annual report 2004:16.

²⁹⁸ Steinhoff annual report 2004:17.

²⁹⁹ <https://www.companieshistory.com/steinhoff-international> Accessed 17/10/2020.

³⁰⁰ <https://www.companieshistory.com/steinhoff-international> Accessed 17/10/2020.

³⁰¹ <https://www.companieshistory.com/steinhoff-international> Accessed 17/10/2020.

³⁰² Moorad 2011:1.

³⁰³ <https://www.companieshistory.com/steinhoff-international> Accessed 17/10/2020.

2013: Acquired Slumberland, Myers, Dunlopillo, Staples.³⁰⁴

2014: The results were lower supply chain costs in Eastern Europe, Australia and Africa. Steinhoff started to prioritise e-commerce to expand the brands.³⁰⁵ Acquired Kika-Leiner (through Genesis) through Conforama and acquired assets from Fly, Atlas and Crozatier.

The largest acquisition made by Steinhoff was in November 2014 when Steinhoff acquired a 93,34% stake in Pepkor from Christo Wiese for R62.8 billion³⁰⁶ without issuing a cautionary announcement whereby shareholders are informed about the impact of the transaction on the share price.³⁰⁷ Investigative journalist Theophilous (Theo) Botha probed Steinhoff's decision not to issue a cautionary announcement during the Steinhoff AGM on 2 December 2014.³⁰⁸ The decision not to issue a cautionary announcement was not illegal or irregular, according to JSE rules. Still, it just seemed strange that in such an instance of a business deal that had the potential to change the entire corporate strategy, no cautionary announcement was issued in contrast with the seller Brat Group that issued a cautionary announcement.³⁰⁹ This transaction made Wiese one of Steinhoff's largest shareholders. Shortly before the finalisation of the Pepkor transaction, Steinhoff board members jointly bought shares of about R120 million. Questions may be asked whether the shareholders who sold their shares had the same information as those who bought shares, whether the Steinhoff directors had prior knowledge of the transaction, or whether it was purely incidental.³¹⁰

2014: As indicated by Styan in 2014, Steinhoff bought shares in the JD Group that was 38% more than the worth of the JD Group's shares in the preceding six months; the JD Group announced a net loss of R138 million³¹¹ and increased its interest in JD Group and KAP.³¹²

³⁰⁴ [https://www.bigbrandbeds.co.uk/blog/steinhoff-buys-myers-dunlopillo-staples-and-slumberland-bed-brands/Steinhoff annual report 2004:17](https://www.bigbrandbeds.co.uk/blog/steinhoff-buys-myers-dunlopillo-staples-and-slumberland-bed-brands/Steinhoff%20annual%20report%2004:17) Accessed 21/11/2020.

³⁰⁵ Steinhoff annual report 2014:16.

³⁰⁶ <https://www.fin24.com/Companies/Retail/Steinhoff-to-buy-Pepkor-stake-in-R682bn-deal-20141125> Accessed 8/3/2019.

³⁰⁷ Styan 2018:92.

³⁰⁸ Styan 2018:93.

³⁰⁹ Butters 2019:29.

³¹⁰ Styan 2018:92.

³¹¹ Styan 2018:91.

³¹² Steinhoff annual report 2014:3.

2015: Steinhoff launched the Pep & Co. brand in the UK,³¹³ and primarily listed on the Frankfurt Stock Exchange (FSE) in Germany. The most significant merger was in 2016 with Mattress Firm in the US.³¹⁴ At the height of its success, Steinhoff was part of the JSE Top 40 index, the JSE Top 25 Industrial index and the JSE Socially Responsible Investment (SRI) index.³¹⁵

Over the last few years, observers became concerned about the spree of acquisitions, the high levels of complexity associated with these acquisitions, and the company's ability to acquire ailing businesses and (nearly instantaneously) show improved results once these businesses have been incorporated into the group.³¹⁶ 26 November 2015 German authorities searched Steinhoff Europe group services offices relating to a review of balance sheet items.³¹⁷

4 December 2015 confirmation of dispute with partners Steinhoff announces that these authorities found no evidence of any contravention of any provision of German commercial law.³¹⁸

2016: Through Pepkor, acquired GHM, Tekkie Town and acquired Iliad, including the Buce brand, Poundland, and Fantastic Holdings Group (Australia).³¹⁹

2017: the company had become a global retail giant. Business categories included decoration, furniture, consumer electronics, cellular, kitchen, bathroom, quick-fix essentials, kitchens, appliances, clothing, footwear, beds and mattresses that controlled a fully integrated supply chain which included sourcing, distribution, logistics and retail.³²⁰ Its integrated retail business is spread across the following regions i) UK: (Harveys, Bensons for Beds, Cargo); ii) Asia Pacific: (Freedom, Snooze, Poco) and iii) Africa: (JD furniture

³¹³ <https://www.news24.com/auth/information/legacybrowser> Accessed 21/11/2020.

³¹⁴ Hogg 2016:1.

³¹⁵ Naude et al 2018:9.

³¹⁶ Wild et al 2017:1.

³¹⁷ Rossouw et al 2019:163.

³¹⁸ <https://viceroyresearch.files.wordpress.com/2017/12/steinhoff-article-viceroy2.pdf> Accessed 21/11/2020.

³¹⁹ <https://www.africaglobalfunds.com/news/private-equity/exits/steinhoff-buys-actiss-stake-in-tekkie-town> Accessed 1/11/2020.

³²⁰ Naude et al 2018:8.

brands, Poco, Incredible Connection, Hi-Fi Company, Pennypinchers, Timbercity, Hardware Warehouse, The Tile House); and its global brands Bensons for Beds (household goods); Poundland (general merchandise); Pep & Co. (general merchandise); GHM! (general merchandise), are known in the UK. Its integrated retail business is also spread across the following regions iv) Europe, Poco (household goods); Conforama (household goods); kika-Leiner (household goods); Pepco (general merchandise); v) Africa, PEP (general merchandise); Ackermans (general merchandise); Russells (household goods); Incredible Connection (household goods); Unitrans (auto). vi) Australia and New Zealand: Freedom (household goods); Best & Less (general merchandise); Harris Scarfe (general merchandise); and Snooze (household goods).

23 August 2017 Manager-Magazine reports that Markus Jooste was among employees under investigation by German prosecutors in relation to accounting fraud (in 2015).

24 August 2017 Steinhoff denies the Manager-Magazine claims as “wrong or misleading”.

5 December 2017 Steinhoff announces a delay in releasing audited financial statements due to pending investigations.³²¹

6 December 2017, Steinhoff announced the resignation of Markus Jooste (CEO) and that PricewaterhouseCoopers has been appointed to investigate possible “accounting irregularities”. Steinhoff International Holdings’ share price plunged by 60%,³²² causing a €10 billion loss in shareholder value.³²³ A New York investor group issued the Viceroy Research report the same day.³²⁴

9-11 December 2017 The company establishes an independent board sub-committee to improve independent governance: Christo Wiese is appointed Executive Chairman by the Supervisory Board, and Pieter Erasmus in an executive advisory capacity.³²⁵ The board

³²¹ <https://www.southwood.co.za/steinhoff-note> Accessed 21/11/2020.

³²² <https://www.moneyweb.co.za/news/companies-and-deals/steinhoff-ceo-markus-jooste-quits> Accessed 09/03/2019.

³²³ <https://accountingweekly.com/why-steinhoffs-board-needs-to-be-held-accountable> Accessed 09/03/2019.

³²⁴ <https://viceroyresearch.org/wp-content/uploads/2017/12/steinhoff-article-viceroy2.pdf> Accessed 11/4/2.21.

³²⁵ Rossouw 2018:1.

comprises Dr Johan van Zyl, Dr Steve Booyesen and Heather Sonn.³²⁶ Wiese attempts to stabilise the company.³²⁷

14 December 2017 Wiese, a board member since 2013 and Chairman since 2016, resigned as Chairman of the board because shareholder PIC³²⁸ expressed concern about the possible conflict of interest in having Wiese as interim chief Executive.³²⁹

On 19 December 2017, Steinhoff supervisory board consisting of Johan van Zyl, (former Sanlam CEO), Steve Booyesen (former Absa CEO) and Heather Sonn, who replaced Christo Wiese as the group's chairperson, made three new appointments to the management board, Daniel van der Merwe (former COO) is promoted as acting CEO, a deputy director Alexandre Nodale (acting Group Deputy CEO who also continues as CEO of Conforama) is appointed and Louis du Preez as Group Commercial Director.³³⁰ Heather Sonn acknowledged accounting irregularities and confirmed the company's priorities to finalise a restructuring plan and the 2017 audit.³³¹

In South Africa, public entities were severely affected by the collapse. These include the PIC,³³² which manages the funds of the GEPF,³³³ among other public entities. The PIC is reported to hold 10% of Steinhoff's total shares, meaning its losses reached more than R10 billion after the share price collapsed.³³⁴ Under the watch of the Steinhoff board of directors, a massive corporate collapse occurred, leading to massive destruction in shareholder value.³³⁵

3. TIMELINE OF THE INVESTIGATIONS

³²⁶ <https://www.pmg.org.za> Accessed 21/11/2020.

³²⁷ <https://businesstech.co.za/news/business/215761/wiese-in-bid-to-save-steinhoff/> Accessed 21/11/2020.

³²⁸ Public Public Investment Corporation

³²⁹ <https://www.reuters.com/article/us-steinhoff-intl/nl-chairman-idUSKBN1E82SH> Accessed 22/11/2020.

³³⁰ <https://www.timeslive.co.za/sunday-times/business/2017-12-19-beleaguered-steinhoff-reshuffles-the-desk-chairs/> Accessed 22/11/2020.

³³¹ Khumalo 2020:1.

³³² Public Investment Company

³³³ Government Employees Pension Fund

³³⁴ <https://www.wits.ac.za/news/latest-news/in-their-own-words/2017/2017-12/steinhoff-scandal-points-to-major-gaps-in-stopping-unethical-corporate-behaviour.html> Accessed 22/8/2020.

³³⁵ <https://www.wits.ac.za/news/latest-news/in-their-own-words/2017/2017-12/steinhoff-scandal-points-to-major-gaps-in-stopping-unethical-corporate-behaviour.html> Accessed 22/8/2020.

Currently, Steinhoff faces investigations or legal actions instituted by various bodies and authorities, including JSE,³³⁶ FSB,³³⁷ DTI³³⁸ and CIPC.³³⁹ Steinhoff is charged in civil suits in three countries, Germany, the Netherlands and Austria, by former business partner Andreas Seifert.³⁴⁰

2018: On 31 January 2018, Steinhoff management appeared in a joint briefing before the Parliamentary committee regarding the Steinhoff crisis. The briefing included the Standing Committee on Finance, Standing Committee on Public Accounts and Portfolio Committee on Public Service and Administration, together with National Treasury, the South African Reserve Bank (SARB), the Johannesburg Stock Exchange (JSE), the Financial Services Board (FSB), the Public Investment Corporation (PIC), Government Employees Pension Fund (GEPF), and the Independent Regulatory Board for Auditors (IRBA).³⁴¹

On 2 February 2018, Steinhoff announced the board resignations: of Mariza Nel, Stephanus Johannes Grobler and Thierry Guilbert. PIC voted for the removal of Len Konar from the board.³⁴²

On 5 February 2018, VEB³⁴³ filed a lawsuit against the company, stating that it published “inaccurate and misleading information”. On 15 February 2018, Steinhoff appointed an independent external expert Richard Heis as Chief Restructuring Officer to the board.³⁴⁴

During April 2018, at the AGM, various board appointments were made. Five new members were appointed to the Supervisory Board: Khanyisile Kweyama, Moira Moses, Hugo Nelson, Peter Wakkie and Alexandra Watson and retained Stefanus Booysen, Angela Krüger-Steinhoff and Heather Sonn. Johan van Zyl resigns from the Supervisory Board.³⁴⁵ The Management Board appoints Philip Dieperink (Chief Financial Officer),

³³⁶ Johannesburg Stock Exchange

³³⁷ Financial Services Board

³³⁸ Department of Trade and Industry

³³⁹ Companies and Intellectual Property Commission

³⁴⁰ <https://www.bloomberg.com/news/articles/2017-12-19/steinhoff-fights-lawsuits-in-three-countries-as-crisis-continues> Accessed 22/11/2020.

³⁴¹ <https://pmg.org.za/committee-meeting/25753> Accessed 21/11/2020.

³⁴² Crotty 2018:12

³⁴³ Dutch Vereniging van Effectenbezitters

³⁴⁴ <https://www.marketwatch.com/story/steinhoff-appoints-chief-restructuring-officer-2018-02-15> Accessed 22/11/2020.

³⁴⁵ Naude et al 2018:11.

Theodore de Klerk (Operational Director), Alexandre Nodale (Deputy Chief Executive Officer) and Louis du Preez (Commercial Director).³⁴⁶

Deloitte Accountants B.V. has been reappointed as the external auditor for the financial year 2018.³⁴⁷

In January 2018, the CIPC³⁴⁸ issued Steinhoff with a compliance notice wherein Steinhoff was to identify the individuals involved in falsifying records to enable CIPC to institute criminal and civil action.³⁴⁹

On 30 August 2018, an oversight meeting was held by The Standing Committees on Finance; the Standing Committee on Public Accounts (Scopa); the Portfolio Committees on Trade and Industry and; the Portfolio Committee on Public Service and Administration, the Steinhoff supervisory board and management, former Steinhoff Chief Executive Officer, Mr Ben La Grange, the Johannesburg Securities Exchange, Companies and Intellectual Properties Commission, Financial Services Conduct Authority, Independent Regulatory Board for Auditors and the Hawks.³⁵⁰

Steinhoff International Holdings complied with the compliance notice and issued a certificate of compliance in September 2018.³⁵¹

2019: In March 2019, PWC³⁵² released a report regarding fraud allegations and suspicious transactions. According to Business Insider SA,³⁵³ Steinhoff confirmed that transactions were done with companies that were supposed to be independent third parties but had links with Jooste, and transactions such as buying trademarks from Steinhoff at inflated prices were identified.³⁵⁴ Steinhoff granted massive loans to companies with links with

³⁴⁶ <https://www.steinhoffinternational.com/downloads/2018/latest-results/Half-year/report/202018.pdf>
Accessed 22/11/2020.

³⁴⁷ Naude et al 2018:12.

³⁴⁸ Companies and intellectual property commission

³⁴⁹ DPCI report 2019:6.

³⁵⁰ <https://www.parliament.gov.za/press-releases/hawks-need-act-urgently-steinhof-matters-committes>
Accessed 22/11/2020.

³⁵¹ <https://www.thedtic.gov.za/wp-content/uploads/CIPC-STEINHOFF.pdf> Accessed 24/11/2020.

³⁵² PriceWaterhouseCoopers

³⁵³ <https://www.businessinsider.co.za/new-steinhoff-report-2019-3> Accessed 24/11/2020.

³⁵⁴ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> Accessed 02/03/2021.

Jooste, thereby buying its assets.³⁵⁵ According to the report, three groups of companies, The Champion/Fulcrum group, The Talgarth Group and the TG Group, are suspected of having been involved in the fraudulent transactions.³⁵⁶

During May 2019 and June 2019, the delayed 2017 and 2018 annual reports were published.³⁵⁷ In August 2019, the financial restructuring of Steinhoff and the disposal of assets to restructure the debt commenced.³⁵⁸ The financial recovery process involved different teams in different processes, which included specialist legal and financial advice.

On 4 September 2019, a presentation was given by the DPCI³⁵⁹ to the SCOF³⁶⁰ to apprise the SCOF of the investigation relating to Steinhoff international holding. The presentation was a joint compilation by the DPCI and NPA.³⁶¹ The Serious economic offences unit conducts the investigations, and the investigation team has seven members and multidisciplinary partners FSCA,³⁶² AFU,³⁶³ FIC,³⁶⁴ SARB,³⁶⁵ JSE,³⁶⁶ CIPC³⁶⁷ and IRBA.³⁶⁸

Four complaints were received as of 4 September 2019, combined into one criminal investigation.³⁶⁹ The allegations are that Steinhoff Investment Holdings LTD (SA) has been submitting false, misleading and/or deceptive financial statements to attract investors in contravention of the Financial Markets Act.³⁷⁰

2020: On 19 March 2020, PwC³⁷¹ released a forensic report which uncovered €6.5 billion in fictitious and irregular transactions.³⁷² It now appears that similar to Enron, Steinhoff

³⁵⁵ <https://www.businessinsider.co.za/new-steinhoff-report-2019-3> Accessed 24/11/2020.

³⁵⁶ <https://www.businessinsider.co.za/new-steinhoff-report-2019-3> Accessed 24/11/2020.

³⁵⁷ <https://www.smag.co.za> Steinhoff press release Accessed 12/11/2020.

³⁵⁸ <https://www.smag.co.za> Steinhoff press release Accessed 11/11/2020.

³⁵⁹ Directorate of priority crime investigation

³⁶⁰ Standing committee on finance

³⁶¹ National prosecuting authority

³⁶² Financial sector conduct authority

³⁶³ Asset forfeiture unit

³⁶⁴ Financial intelligence centre

³⁶⁵ South African reserve bank

³⁶⁶ Johannesburg securities exchange

³⁶⁷ Companies and intellectual commission

³⁶⁸ Independent regulatory board for auditors

³⁶⁹ DPCI report 2019:6.

³⁷⁰ Act 19 of 2012

³⁷¹ Price Waterhouse Coopers

³⁷² Butters 2019:29.

engaged in various complex financial transactions.³⁷³ These complex fictitious transactions overstated the income and asset values and, in some instances, were supported by documents and professional opinions that were created and back-dated.³⁷⁴ In May 2020, Sonn resigned and was succeeded by Moira Moses.³⁷⁵

Since the scandal, numerous legal actions and investigations have been instituted against Steinhoff, which includes an R59 billion claim by Christo Wiese, a former chairman and top shareholder, a class action suit from Dutch shareholders rights group VEB, since 2015, the state prosecutor in Oldenburg Germany has been investigating suspected accounting irregularities and criminal investigations by the Hawks police unit.³⁷⁶ Currently, the standing committee on finance of the parliament of the Republic of south Africa is awaiting feedback from regulatory agencies and law enforcement agencies on the Steinhoff debacle.³⁷⁷

In October 2020, the JSE fined Steinhoff R13,5 million for breaching listing requirements and publishing false information. The FSCA³⁷⁸ fined Jooste R162 million for sending SMS warnings about Steinhoff's share price to four friends (insider trading). He was also ordered to pay the investigation costs and is jointly liable for R56 million in fines issued to the recipients of the SMSes.³⁷⁹ Jooste is taking the matter on review to the Financial Sector Tribunal³⁸⁰.

According to Steinhoff's Annual Report 2020, claw-back proceedings were instituted on the 14th of June 2019 against Jooste and Ben La Grange³⁸¹ for the repayment of annual bonuses, special project bonuses, irregular payments and the value of shares awarded to them for the period 2009 to the date of their termination. Claw-back claims have not been instituted against any current Managing Board Directors or Supervisory Board Directors.

³⁷³ Schwarcz 2002:1309.

³⁷⁴ Steinhoff annual report 2020:18.

³⁷⁵ <https://www.news24.com/fin24/companies/retail/just-in-steinhoff-chairperson-heather-sonn-has-resigned> Accessed 20/8/2020.

³⁷⁶ <https://in.reuters.com/article/us-steinhoff-intln-accounts/pwc-investigation-finds-74-billion-accounting-fraud-at-steinhoff-company-says-idINKCN1QW2C2> Accessed 02/10/2020.

³⁷⁷ <https://www.pmg.org.za/taled-committee-report> Accessed 12/11/2020.

³⁷⁸ Financial Sector Conduct Authority

³⁷⁹ <https://mg.co.za/business/2020-10-30-financial-conduct-body-slaps-jooste-with-r162-million-fine/> Accessed 02/11/2020.

³⁸⁰ The tribunal was established in 2019 to reconsider the findings of the FSCA and various ombuds.

³⁸¹ Former chief financial officer

Jooste is defending this matter.³⁸² Since the discovery of the accounting fraud scandal in December 2017, a settlement proposal has been developed pending the acceptance of regulators, creditors and claimants.

2021: In January 2021, the Western Cape High Court granted a court order³⁸³ regarding the proposed scheme of arrangement and compromise relating to Steinhoff International Holdings Proprietary Limited and the Section 155 proposal. On 24 March 2021, Trevo Capital and others³⁸⁴ brought an application to intervene in a declaratory application brought by Steinhoff International Holdings (Pty) Ltd. The court ordered that if any other creditor or potential creditor of Steinhoff International Holdings (Pty) Ltd intends to apply to intervene in the declaratory application, such creditor or potential creditor is to file its intervention application with a supporting affidavit within fifteen (15) court days after deemed receipt of the notice.

4. DEVELOPMENTS AFTER MARCH 2021

In March 2021, German authorities confirmed that fraud charges were laid against former Steinhoff executives.³⁸⁵ On March 3 2021, the South African minister of justice and correctional services, Raymond Lamola, informed parliament that the National Prosecuting Authority has not yet completed the investigation.³⁸⁶

On 14 March 2021, Louis du Preez, the CEO of Steinhoff, announced that R30 million be made available to PwC to assist with the forensic investigation.³⁸⁷ This payment raised numerous concerns ranging from Steinhoff's breaching of its fiduciary duties toward the thousands of victims who lost money due to the alleged fraudulent corporate transactions. What is the legal purpose, and how does it relate to Steinhoff's core business of giving R30 million to the State?

³⁸² Steinhoff annual report 2020:85.

³⁸³ Case no 16337/2020

³⁸⁴ Trevo Capital and others in re: *Hali BV and others* case no 17327/2020 WCC

³⁸⁵ <https://www.news24.com/fin24/companies/breaking-german-prosecutors-charge-3-former-steinhoff-execs-for-balance-sheet-fraud-20210304> Accessed 05/03/2021.

³⁸⁶ <https://www.moneyweb.co.za/news/companies-and-deals/steinhoff-first-criminal-charges-loom/> Accessed 04/03/2021.

³⁸⁷ <https://www.iol.co.za/sundayindependent/dispatch/Whichever-way-you-look-at-it,-that-R30m-Steinhoff-gift-is-dodgy/> Accessed 23/03/2021.

31 March 2021 Burford Capital, Deminor Recovery Services, and DRRT/Therium recommended that their constituents, which include South African investors, support Steinhoff's proposed settlement of €943 million (roughly R17 billion) to be split among all claimants, who have been divided into contractual and market purchase claimants.³⁸⁸ The voting deadline for claimants was 5 May 2021.³⁸⁹

In April 2021, Mayfair Speculators sued Jooste and Steinhoff for R4 billion, a claim that relates to 20 million shares in investment holding company PSG, which it swapped for cash and Steinhoff shares in late 2011. During 2011 Jooste was The CEO of Steinhoff and a director of Mayfair.³⁹⁰ Jooste and Steinhoff are defending the matter.

On 11 May 2021, the former owners of Tekkie Town brought an urgent application for the liquidation of Steinhoff in the Western Cape High Court and also voted against the settlement proposal.³⁹¹ In the same month, the South African Institute of chartered accountants charged Jooste with several misconduct charges, which included non-compliance with the Companies Act and Financial Markets Act, non-disclosure of accounting irregularities, bringing the profession of accountancy into disrepute by behaving dishonourable and dishonestly and breaching his obligation to act with integrity and objectivity.³⁹²

In June 2021, Lancaster 101 abandoned a court bid against Steinhoff's proposed settlement.³⁹³

³⁸⁸ <https://www.news24.com/fin24/companies/retail/steinhoff-says-four-large-investor-groups-support-r17bn-settlement-proposal-20210331> Accessed 23/6/2021.

³⁸⁹ <https://www.news24.com/fin24/companies/has-your-steinhoff-claim-been-submitted-as-deadline-nears-now-is-the-time-to-check-20210504> Accessed 08/07/2021.

³⁹⁰ <https://www.news24.com/fin24/companies/markus-jooste-sued-for-r4-billion-by-his-former-horse-racing-company-over-2011-share-swap-20210430> Accessed 08/07/2021.

³⁹¹ <https://www.news24.com/fin24/companies/retail/steinhoff-vows-to-vigorously-defend-settlement-proposal-in-wake-of-liquidation-bid-20210513> Accessed 08/07/2021.

³⁹² <https://www.dailymaverick.co.za/article/2021-05-24-accounting-watchdog-saica-charges-ex-steinhoff-ceo-markus-jooste-with-isconduct> Accessed 28/05/2021.

³⁹³ <https://www.businesslive.co.za/lancaster-drops-drops-steinhoff-action> Accessed 03/07/2021.

In September 2021, a liquidation application³⁹⁴ was brought to the Western High Court by former Tekkie Town owners.³⁹⁵ The application was opposed by SIHNV financial creditors³⁹⁶ and Frederic Verhoeven and Christiaan Robert Zijderveld³⁹⁷ based on the argument that Steinhoff is an external company established in the Netherlands and cannot be liquidated in South Africa in terms of the Companies Act.³⁹⁸ The court ruled that the South African courts have jurisdiction to hear the liquidation application of an external company registered in a foreign country.³⁹⁹ Most institutional investors and financial and market purchase claimants voted in favour of a settlement proposal made by Steinhoff.⁴⁰⁰

In October 2021, Steinhoff applied for leave to appeal in the Constitutional Court against the Western High Court, ruling that it has jurisdiction over the liquidation application in South Africa.⁴⁰¹ During Oct 2021, proceedings were instituted against Jooste and Le Grange for the repayment of remuneration paid to them from 2009 to 2017/2018 in their capacities as senior executives of the collectively referred to as the "Steinhoff companies".⁴⁰²

In the matter of *Tiso Blackstar Group and others vs Steinhoff international holdings*⁴⁰³ on 31 January 2022, the Western Cape High Court granted an application to access the PWC report held by Steinhoff. The application was brought in terms of Section 53 (1) of the Promotion to Access to Information Act (PAIA).⁴⁰⁴ The court ordered Steinhoff to provide the applicant with a copy of the PWC report.⁴⁰⁵

³⁹⁴ <https://www.moneyweb.co.za/news/companies-and-deals/liquidation-proceedings-against-steinhoff-can-proceed> Accessed 03/07/2021.

³⁹⁵ <https://bd.pressreader.com/article/281767042342422> Accessed 10/09/2021.

³⁹⁶ A group representing Steinhoff International.

³⁹⁷ Two Dutch administrators who were administering settlement proceedings on behalf of Steinhoff in the Netherlands.

³⁹⁸ 71/2008.

³⁹⁹ <https://www.citizen.co.za/business/business-news/2614451/steinhoff-liquidation-can-be-decided-in-sa-court> Accessed 06/09/2021.

⁴⁰⁰ <https://bd.pressreader.com/article/281487869461817> Accessed 28/05/2022.

⁴⁰¹ <https://www.news24.com/fin24/companies/consourt-refuses-to-hear-steinhoffsgid-to-appeal-ruling-on-liquidation-case-20211015> Accessed 28/5/2022.

⁴⁰² *Steinhoff International Holdings v Jooste and Another* 2021 ZAWCHC 222: par 1.

⁴⁰³ *Tiso Blackstar group v Steinhoff International Holdings* 2019 SA 1 W:4.

⁴⁰⁴ Promotion to Access to Information Act 2/2000.

⁴⁰⁵ *Tiso Blackstar v Steinhoff*:27.

In November 2019, the Competition Commission of SA referred a complaint of collusive price fixing regarding the Competition Act⁴⁰⁶ against Steinhoff International to the Competition Tribunal. An application for review was brought by *Steinhoff International Holdings NV v The Competition Commission of SA*,⁴⁰⁷ and the Gauteng High Court granted the application for review on 26 January 2022.

During May 2022, it was reported that Steinhoff had received more than 43000 claims from investors and pension funds. Since December 2017, more than 100 lawsuits worth R180 billion from investors have been initiated.⁴⁰⁸

During August 2022, the JSE alleged that a handwritten invoice of R376m that Jooste presented to the then CFO in 2016 created the impression that money was owed and paid for work done and was an entirely fictitious transaction. The handwritten invoice also formed part of the application brought by the South African Reserve Bank ("SARB").

In October 2022, SARB brought an application in the Western Cape High Court against Jooste to preserve assets on suspicion of contravention of exchange control laws.⁴⁰⁹ The court granted the application and issued an attachment order to attach Steinhoff-related assets. It is alleged that Jooste and various entities in the Steinhoff stable contravened regulations governing permission to send or earn funds abroad. Assets (including property, motor vehicles and an art collection) of Jooste were attached. The assets of other former Steinhoff executives were also attached.

In April 2023, Jooste and a co-accused had to appear in Germany on five charges of violations of Section 331 of Germany's commercial law, which involves fraud, including false representation of financial statements and manipulating accounts. This is the first

⁴⁰⁶ Competition Act 89/1998.

⁴⁰⁷ *Steinhoff international holdings vs The Competition Commission of South Africa* case no 22310/2020 unreported

⁴⁰⁸ <https://www.businesslive.co.za/steinhoff-receives-more-than-43,000-claims-in-first-of-its-kind-payout> Accessed 22/5/2022.

⁴⁰⁹ <https://www.news24.com/fin24/companies/just-in-sa-reserve-bank-hits-markus-joostes-hermanus-house-lanzerac-20221018> Accessed 12/12/2022.

criminal charge against Jooste since the Steinhoff collapse.⁴¹⁰ However, Jooste failed to appear in court. The investigation is still pending in South Africa to date.

In Germany, the Steinhoff collapse has been described as the second-largest accounting scandal in its history. Steinhoff's primary listing is in Germany, and the financial irregularities that were investigated during the financial forensic investigation also resulted in huge financial losses for German pension funds and investors.

⁴¹⁰ <https://www.news24.com/fin24/companies/markus-jooste-trial-in-germany-what-you-need-to-know>
Accessed 18/04/2022.

CHAPTER 4: SOUTH AFRICA

1. INTRODUCTION

This chapter will set out the corporate governance structure of South Africa. Corporate collapses in South Africa will be discussed.

2. COMPANIES ACT 70 OF 2008

South Africa's corporate governance law is embedded in English law.⁴¹¹ Common-Law jurisdictions treat the director's duty of care skill and diligence differently from the director's fiduciary duty.⁴¹² The primary legal framework of corporate governance in South Africa is the Companies Act 71 of 2008 (the Act),⁴¹³ common law, codes of best practice such as the King reports, and a company's specific policies and memorandum of incorporation.⁴¹⁴ Regarding corporate governance, Section 7 specifies the purposes of the Act: (a) to ensure compliance with the Bill of Rights as stipulated by the Constitution in the application of company law; and (b).to promote the continued development of the South African economy through increasing transparency and high corporate governance standards.⁴¹⁵ Regulatory agencies are responsible for the enforcement of the Act.⁴¹⁶ These regulatory agencies comprise the Companies and Intellectual Property Commission, the Financial Reporting Standards Council, and the Takeover Regulation Panel.⁴¹⁷

In contrast with the prescriptive rule approach of the United States, both the King Codes I-IV and the JSE corporate listing requirements⁴¹⁸ are not legislated, and compliance is voluntary.⁴¹⁹ The JSE corporate listing requirements apply to all entities listed on the JSE and require entities to report on a "apply and explain" basis on the effectiveness of internal control measures and risk management, as well as disclose their level of King IV Report

⁴¹¹ Lee 2005:50.

⁴¹² Mupangavanhu 2017:148-149.

⁴¹³ The Act came into effect on 1 May 2011 and provides provisions regarding corporate governance.

⁴¹⁴ Parry 2014:18; Lee 2005:68.

⁴¹⁵ Mongalo 2015:23.

⁴¹⁶ Cassim et al 2018:444.

⁴¹⁷ Parry 2014:24.

⁴¹⁸ JSE listing requirement 3.84.

⁴¹⁹ Chauke and Mamokhere 2020:16171; Olson 2010:220-221.

compliance. The enforcement of the Act, together with the JSE listing requirements, ensures accountability and transparency. Companies must report annually on the degree of compliance with the King Code on an "apply and explain" basis.⁴²⁰ However, there are no legal obligations or similar to those in the USA⁴²¹ for companies to adhere to corporate governance codes or enforcement mechanisms.⁴²²

In South Africa, a hybrid system exists as the Act legislates certain aspects of corporate governance, whereas other aspects are governed exclusively by King IV. King IV applies to all companies regardless of their form of incorporation.⁴²³ The law prevails in instances of conflict between legislation and the King Code. The standards for directors' conduct are codified in the Act and enforced by the CIPC, where the standards are not met. The incorporation of companies is simplified in the Act into one Memorandum, which sets out the duties, rights and responsibilities of directors, shareholders and other stakeholders.⁴²⁴ High standards of corporate governance are encouraged, and transparency will ensure greater director accountability. Shareholder and stakeholder participation are improved.

3. KING REPORTS I-IV

3.1 INTRODUCTION

McGregor observed that the most influential initiative in developing corporate governance concepts and practices in South Africa was the King Reports.⁴²⁵ All of the reports provide principles and best practice recommendations, including social and environmental responsibility.⁴²⁶ Lee noted that the King reports predominantly focus on the systems by which corporations are managed and controlled and the communications between corporations and shareholders.⁴²⁷ Lee further identified seven characteristics of good corporate governance: responsibility, discipline, fairness, independence, transparency,

⁴²⁰ The apply and explain basis is similar to the self-explanatory approach in the UK. Dbe 2003:282.

⁴²¹ Non-compliance is regulated in the Sarbanes-Oxley Act of 2002.

⁴²² Parry 2014:17.

⁴²³ Wiese 2018:22.

⁴²⁴ McGregor 2011:399.

⁴²⁵ McGregor 2011:392.

⁴²⁶ McGregor 2011:393.

⁴²⁷ Lee 2005:50-51.

social responsibility and accountability that have been implemented throughout the King reports.⁴²⁸

The King Report recommended that the South African Standing Advisory Committee on Company Law determine whether a statutory business judgement rule ("BJR") is required.⁴²⁹ The business judgment rule was defined in the King Report as a rule that "*protects directors against being held accountable for business decisions, however unwise they subsequently turn out to be.*"⁴³⁰ The recommendation came amongst a growing concern of recent corporate collapse that would result in a greater tendency to impose stricter liability on company directors for breach of their common law duties where their actions have caused financial harm to the company.⁴³¹ Directors have clothed authority to manage the company dynamically, with entrepreneurial flair, by engaging in responsible, competitive risk-taking within the corporate governance framework and maximizing returns to shareholders.⁴³² According to Mupangavanhu, corporate governance in South Africa was institutionalised between 1994 and 2009 with the publication of the King reports..⁴³³

The King Reports advocated that companies use the inclusive stakeholder approach that is fundamental for companies to succeed at balancing economic efficiency and the broader objectives of society.⁴³⁴ The King reports influenced the development of global corporate governance principles, business practices, and government policies.⁴³⁵

3.2 THE KING COMMITTEE

⁴²⁸ Lee 2005:51-52.

⁴²⁹ King Report II 2002:73. Walter 1988:649.

⁴³⁰ King Report I 1994:9.

⁴³¹ Corporate collapses included MacMed, Leisurenent and Regal Treasury Bank. Lee 2005:51.

⁴³² Lee 2005:50.

⁴³³ Mupangavanhu 2016:31.

⁴³⁴ Jebe et al 2018:136.

⁴³⁵ Jebe et al 2018:138; Lee 2005:50-51.

The King Committee was formed in 1992 at the instance of the Institute of Directors of Southern Africa ("IoD"),⁴³⁶ following the Cadbury report in the UK in 1992.⁴³⁷ Following the collapse of apartheid in 1994 and similar to other Anglo-American countries, proposals on the reform of corporate disclosure were forwarded to the Department of Trade and Industry ("DTI").⁴³⁸ Named after its chairperson, Judge Mervyn King, the King Committee published the King I Report on corporate governance for South Africa, which contained a code of corporate practices and conduct.⁴³⁹ The process of writing the King Reports was highly consultative, and the committees consisted of representatives of significant public, private and professional sector institutions and leading proponents of corporate governance. The IoD assisted in drafting practical guidelines and hosting workshops and seminars on implementing the King Reports. The Code, unlike to codes of SOX, is based on principles and practices and is non-legislative. The Code focuses on sustainability, good corporate citizenship, and leadership.

In 2002 this report was superseded by the King II Report, which also contained a code of corporate practices and conduct.⁴⁴⁰ On 1 March 2010, the King III Report and King Code of Governance for South Africa 2009 (the Code) came into effect and replaced the King II Report and Code of Corporate Practices and Conduct.⁴⁴¹ The King III Report must be read in conjunction with the Code and applies to all entities incorporated and domiciled in South Africa, regardless of the manner and form of incorporation or establishment, and regardless of whether such establishments are in the public, private, or non-profit sectors.⁴⁴² The King Reports articulate, conceptualize, and identify important values and principles required to fulfil the aspirations of the new Constitutional regime.⁴⁴³

3.3 KING I REPORT

⁴³⁶ McGregor 2011:397. Majmudar 2021:78-79 referred to the Naresh Chandra Committee that was established in India in 2002 on corporate audit and governance to investigate corporate governance measures relating to independent audits, board supervision and financial and non-financial disclosures. A National foundation for corporate governance was established by the Ministry of corporate governance to establish a forum for stakeholders, law enforcement agencies, and non-governmental groups and regulators to deliberate on matters relevant to corporate governance.

⁴³⁷ Jebe 2018:134.

⁴³⁸ Ntim et al 2012:85.

⁴³⁹ Cassim et al 2018:272.

⁴⁴⁰ Lee 2005:50-51.

⁴⁴¹ Lee 2005:51.

⁴⁴² King III report:17.

⁴⁴³ Jebe et al 2018:135.

The first King Report ("King I") was released in 1994.⁴⁴⁴ It defined corporate governance as a system by which companies are controlled; it saw the company as a member of society indeed as a "citizen". It codified the standard of governance applicable to all listed companies and other entities and had an integrated approach.⁴⁴⁵

The aim was to consider the stakeholders' legitimate interests and expectations in decision-making.⁴⁴⁶ The application thereof is voluntary and generally not prescribed by law.⁴⁴⁷ It focuses on an integrated approach to good governance that includes the principles of good social, ethical, and environmental practice.⁴⁴⁸ As stated by Bekink,⁴⁴⁹ the challenge faced by drafters was to strike a balance between directors' freedom to manage, accountability, and stakeholders' interests. The recommendations of the King I Report influenced the Act⁴⁵⁰ and the Securities Services Act 2004.⁴⁵¹

3.4 KING II REPORT

Significant corporate failures which led to the demise of South African companies, including Leisure-net, Regal Bank, and Retail apparel group, added momentum to the drafting and publication of the King II Report in 2002.⁴⁵² The King II Report came into operation on 1 March 2002 and applied to companies listed on the Johannesburg Stock Exchange ("JSE") within the South African financial sector and enterprises performing public functions.⁴⁵³ The aim was to "to promote the highest standards of corporate governance in South Africa."⁴⁵⁴ King II Report promotes the "inclusive stakeholder

⁴⁴⁴ The release of the King I coincided with the release of Nelson Mandela from prison and the subsequent coming of power of the African National Congress (ANC); Olson 2010:220.

⁴⁴⁵ "Integrated" corporate governance disclosure approach encourages companies to go beyond the traditional financial aspects of corporate governance disclosure and take into account a number of stakeholder interests as well.

⁴⁴⁶ <https://www.irmagazine.com/case-studies/audience-gris-mervyn-king> Accessed 12/6/2020.

⁴⁴⁷ Bekink 2008:108.

⁴⁴⁸ Rossouw et al 2002:300.

⁴⁴⁹ Bekink 2008:108.

⁴⁵⁰ Section 56 (3) Compelling disclosure of the identity of beneficial owners of shares held by nominees. McGregor 2011:393.

⁴⁵¹ Section 73 (4) of the Securities Services Act 36 of 2004 which deals with the imparting of advice to deal or not to deal in specified securities. Cassim et al 2018:512. McGregor 2011:393.

⁴⁵² Moloi et al 2010:3; Olson 2010:220.

⁴⁵³ IOD 2002:11.

⁴⁵⁴ Lee 2005:51; West 2009:12.

approach" and acknowledges the transition from a single bottom line to a triple bottom line.⁴⁵⁵ The effect of this transition is that companies consider the economic interests and social and environmental factors in their corporate decision-making and bear in mind that the company is ultimately accountable to the body of shareholders.⁴⁵⁶ As stated by McGregor, the King II Report included recommendations relating to the misbehaviour of directors, the recruitment of directors and the importance of independent directors. King II also advocated good board practices, accounting practices and the relationship behaviours of shareholders.⁴⁵⁷ According to Ntim, the best corporate governance practices aim to protect shareholder interests.⁴⁵⁸

Corporate governance is affected by outside forces and cannot exist separately from the law.⁴⁵⁹ In 2003 Dti initiated a broad legislative reform program and published the Guidelines for Corporate Law Reform ("the Guidelines") in May 2004.⁴⁶⁰ The objective was that the Act⁴⁶¹ should give effect to the principles and rights set out in the Bill of Rights of the Constitution and other laws enacted to give effect to that and the interests of stakeholders and shareholders.⁴⁶² In addition, the guidelines proposed greater disclosure of not only financial but also compliance with public-interest legislation.⁴⁶³ The Act resulted from the Guidelines and came into effect on 1 May 2011. It introduced the business judgment rule⁴⁶⁴ and business rescue dispensation, both foreign American concepts.⁴⁶⁵ The Companies Act 46 of 1926 and the Companies Act 61 of 1973, which preceded the Act, were primarily based on English law.⁴⁶⁶

⁴⁵⁵ "Inclusive" corporate governance approach seeks to maintain and strengthen all the Anglo-American (shareholding) features but distinctively requires companies to provide more transparent information on a number of affirmative action and stakeholder laws passed by the ruling ANC on black economic empowerment, employment equity, environment..HIV/Aids and health and safety. McGregor 2011:397. Mupangavanhu 2017:148; West 2009:12-14.

⁴⁵⁶ Jebe et al 2018:136.

⁴⁵⁷ McGregor 2011:393.

⁴⁵⁸ Ntim et al 2012:86.

⁴⁵⁹ IOD 2009:10.

⁴⁶⁰ Wiese 2018:15. Olson 2010:221: remarks that the role of the DTI is to resolve disputes amongst stakeholders and prevent court proceedings.

⁴⁶¹ Companies Act 71 of 2008.

⁴⁶² Mloi 2015:2.

⁴⁶³ Broad-Based Black Economic Empowerment Act and environmental and labour legislation.

⁴⁶⁴ As explained by Walter 1988:649 the business judgment rule is used to determine whether a director has acted with the necessary skill, care and diligence expected from a director in his position.

⁴⁶⁵ Wiese 2018:16.

⁴⁶⁶ Mupangavanhu 2017:148-149 argued that there is a distinction between fiduciary duties and the duty of care skill and diligence.

3.5 KING III REPORT

The King III Report was published in 2009, entitled King Report on Corporate Governance for South Africa and the King Code of Governance Principles.⁴⁶⁷ The King III Report focuses on “apply or explain” sustainability, the interdependency between the responsibilities of business and social and environmental stakeholders.⁴⁶⁸ According to the King III report, a healthy and productive relationship with stakeholders must be maintained while directors are expected to maximize long-term shareholder value.⁴⁶⁹ Directors are accountable to shareholders for the governance and well-being of the company. In instances where directors failed to implement a recommended practice as stipulated in King III, they should be able to explain their reasoning and motivation to shareholders.⁴⁷⁰ In King III reporting, strategy, governance and sustainability were integrated.⁴⁷¹ Concepts from earlier versions of the King Reports, such as ethical and effective leadership, the organization as an integral part of society, integrated annual reports, stakeholder inclusivity, corporate citizenship and sustainable development, remained. Responsible corporate citizenship was defined as attending to the “triple context” of environmental, economic and social issues.⁴⁷²

3.6 KING IV REPORT

The King IV Code on corporate governance forms part of the King IV Report on corporate governance and is issued by the Institute of Directors (IoD) in Southern Africa. It sets out principles and recommended practices to be followed by companies to warrant corporate governance.

The IoD released the King IV Report on 1 November 2016 and effective in respect of financial years starting on or after 1 April 2017, in response to local and international developments. As with its predecessors, the legal status of King IV is that of a set of voluntary principles and practices. King IV is the first outcomes-based code in the world, meaning that implementing the principles of the Code will achieve the four desired

⁴⁶⁷ McGregor 2011:393.

⁴⁶⁸ McGregor 2011:397.

⁴⁶⁹ Fairfax 2008:3

⁴⁷⁰ McGregor 2011:397.

⁴⁷¹ <https://www.irmagazine.com/case-studies/audience-gris-mervyn-king> Accessed 12/6/2020.

⁴⁷² King III report:22.

governance outcomes: good performance, ethical culture, effective control and legitimacy.⁴⁷³ The 75 principles of King III were reduced to only 16 principles in King IV.⁴⁷⁴

The report aims to reinforce corporate governance principles and that each principle is of equal importance and together forms a holistic approach to governance practices,⁴⁷⁵ governance outcomes, philosophies, and principles that have underpinned the other King codes.⁴⁷⁶ Both King III and King IV Reports are connected to the “triple context,” sustainable development and the development of corporate strategy.⁴⁷⁷ The King IV Report applies to all organisations, including public organisations, private organisations, profit- and non-profit organisations.⁴⁷⁸

King IV Code differentiate between principles and practices. Principles are achieved by mindful consideration and application of recommended practices. The report is not only based on principles but also on outcomes.⁴⁷⁹ The outcomes-based approach⁴⁸⁰ focuses on corporate citizenship, sustainable development, stakeholder inclusivity, and integrated thinking and reporting.⁴⁸¹ The report emphasizes "transparency". With the introduction of an "apply and explain",⁴⁸² organizations have to explain to stakeholders not just which corporate governance principles have been adopted by the organisation but also how their application has contributed to the achievement of the desired governance outcomes.⁴⁸³

As explained by Judin, the board must consider six forms of capital: financial capital, human capital, manufactured capital, natural capital, intellectual capital and social and relationship capital, in decision-making, evaluating and corresponding to risks and opportunities and considering performance outcomes.⁴⁸⁴ Annual reports provide pragmatic evidence of a company's corporate governance compliance.⁴⁸⁵ The implementation of the

⁴⁷³ Judin et al 2017:2.

⁴⁷⁴ Judin et al 2017:1

⁴⁷⁵ Langeni 2018 :99.

⁴⁷⁶ <https://afriamat.co.za/documents/PAIA/2018/Afriamat/Application/King/IV> Accessed 10/6/2020.

⁴⁷⁷ King IV 47.

⁴⁷⁸ Langeni 2018 :99.

⁴⁷⁹ Langeni 2018 :100.

⁴⁸⁰ King IV 20 and 27.

⁴⁸¹ King IV 23-26. Marx and Mohammadali-Haji 2014:244.

⁴⁸² In contrast with the King III which required an explanation where certain principles were not implemented.

⁴⁸³ <https://www.pwc.co.za/kingIV> Accessed 07/09/2020. Judin et al 2017:2.

⁴⁸⁴ Judin et al 2017:2.

⁴⁸⁵ Abeysekera 2007:333.

Code will differ for each organization, and the aspirational nature of the Code should motivate corporations to continuously develop and improve governance practices.⁴⁸⁶

South African law comprises of statutory law and common law as modified and interpreted by judicial precedent.⁴⁸⁷ The courts consider all relevant factors and accepted practices in a particular situation. The more widely recommended practices in codes of governance are adopted and regarded as having met the required standard. It becomes more likely the provisions will find their way into jurisprudence to become part of the common law.⁴⁸⁸ The principles and recommended practices should not merely be applied as a "tick box"-exercise. Still, they should be applied proportionally, considering the size of the turnover and the workforce, resources available, and the complexity of its activities, to realize the governance outcomes.⁴⁸⁹ When the Code and best practices recommendations have been applied, a positive statement to this effect should be made to shareholders in the annual report.⁴⁹⁰ The main public regulators of corporate governance are the Companies and Intellectual Property Commission ("CIPC")⁴⁹¹ and the Financial Sector Conduct Authority ("FSCA"). The King Code principles are included in the listing requirements of the Johannesburg Stock Exchange ("JSE"), which enforces stock exchange listing requirements.⁴⁹²

4. BOARD COMPOSITION

The Act appears to favour a unitary board and requires a minimum of three directors for public and state-owned companies.⁴⁹³ As noted by Olson, the Act does not explicitly require nor preclude the possibility of having a board structure with separate executive and non-executive members. Instead, it allows for individuals who hold some other office, title, designation, or similar status with the company to serve on the board as *ex officio*

⁴⁸⁶ <https://afrimat.co.za/documents/PAIA/2018/Afrimat/Application/King/IV>. Accessed 10/6/2020.

⁴⁸⁷ *De Bruyn v Steinhoff International Holdings* 2022 2 SA 442 GJ:par 132.

⁴⁸⁸ <https://www.pwc.co.za/kingIV> Accessed 07/09/2020.

⁴⁸⁹ King IV 37.

⁴⁹⁰ IOD 2009:8.

⁴⁹¹ Responsible for company law corporate governance requirements such as the functioning and composition of the audit committee.

⁴⁹² OECD 2021:59.

⁴⁹³ Section 66 (1). Olson 2010:227-228 noted that requires a single director for non-public companies.

members.⁴⁹⁴ Independent board members must oversee the company's activities in the best interest of the company and without a conflict of interest.⁴⁹⁵ The Act requires an audit committee and permits additional committees.⁴⁹⁶ The Minister of Trade and Industry may require social and ethics committee or other committees. The Act contains the common law fiduciary duties of directors.⁴⁹⁷ The Act specifies the rules for the appointment of directors.⁴⁹⁸, the removal of directors,⁴⁹⁹ the disqualification of prospective directors,⁵⁰⁰ the remuneration of directors,⁵⁰¹ and the grounds and procedure for declaring or placing directors on probation.⁵⁰² The position of the director has been compared to that of an agent trustee or a managing partner. However, a director is in a *sui generis* relationship with the company.⁵⁰³

As confirmed in *Cohen v Segal*,⁵⁰⁴ the director's relationship with the company must be determined based on the specifics of each case. Insofar as the Act has not limited them, the director's duties under common-law fiduciary duties remain in effect.⁵⁰⁵ The board must ensure that all corporate reports, including annual reports containing information regarding corporate governance policy and the implementation thereof, are correct, comply with legal requirements, and meet the information requirements of shareholders. The board must ensure that integrated reports, annual financial statements and corporate governance disclosures are available to material stakeholders.⁵⁰⁶

4.1. DUTIES OF DIRECTORS

⁴⁹⁴ Section 66 (4). Barlow 2019:1 explains that ex officio members are individuals who serve on a board or committee by virtue of holding another position, such as an executive or managerial role within the corporation. Their membership is automatic and not based on a separate election or appointment process. The notion refers to the position the ex officio member holds, rather than the individual that holds the position.

⁴⁹⁵ Krackhardt 2005:338; Lee 2005:68-71.

⁴⁹⁶ Section 72 (1).

⁴⁹⁷ Sections 75, 76, 77 and 78 of the Act.

⁴⁹⁸ Section 66 (4).

⁴⁹⁹ Section 71.

⁵⁰⁰ Section 162 (5).

⁵⁰¹ Section 66 (8).

⁵⁰² Section 162 (5).

⁵⁰³ Cassim et al 2018:241.

⁵⁰⁴ *Cohen v Segal* 1970 (3) SA 702 W:706B-F.

⁵⁰⁵ Muswakwa 2013:25; Lee 2005:69.

⁵⁰⁶ Lee 2005:68.

Until the 2008 Companies Act, the South African corporate legislation did not contain provisions dealing with the duties of a director.⁵⁰⁷ As stated by Mupangavanhu, prior to enacting the Companies Act 2008, the duties of directors were derived mainly from sources such as the common law,⁵⁰⁸ the Companies Act 61 of 1973, the memorandum of articles and the memorandum of association and the directors' contracts.⁵⁰⁹ Esser and Du Plessis explain:

*[that] "the directors' duties included fiduciary duties and obligations of care, skill and diligence in terms of the common law and various statutory provisions in the Companies Act 61 of 1973."*⁵¹⁰

These statutory provisions either required that directors must do certain things or prevented them from certain acts.⁵¹¹ It also included duties based on the articles of association or even separate agreements between directors and their companies.⁵¹²

According to Delpont,⁵¹³ section 1 of the Act defines a director as a member of the board of a company as contemplated in Section 66 of the Act. It includes any person occupying the position of a director or alternate director⁵¹⁴ by whatever name is designated.⁵¹⁵ According to Cassim, the substance of a person's activities will deem if a person (even if he is described as a manager) is a director, whether with or without lawful authority.⁵¹⁶ Directors play a crucial role in managing the company, as evidenced by the Act, King III and IV Reports, and the King Codes of Governance.⁵¹⁷ The duties and liabilities of directors

⁵⁰⁷ Esser and Du Plessis 2007:346.

⁵⁰⁸ Mupangavanhu 2016:150 noted that Common law is often referred to as principles of law developed through a system of precedents. For example see *Bellairs v Hodnett* 1978 1 SA 1109 (A):1126-1134; *Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd* 1981 2 SA 173 (T):197-199; *Fisheries Development Corporation of SA Ltd v Jorgensen, Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd* 1980 (4) SA 156 (W): 163; *Sibex Construction (SA) (Pty) Ltd v Injectaseal CC* 1988 2 SA 54 (T): 64; *Howard v Herrigel* 1991 2 SA 660 (A) 678; *S v Pouroulis* 1993 4 SA 757 (W):604; *Du Plessis v Phelps* 1995 4 SA 165 (C):170; *Cyberscene Ltd v i-Kiosk Internet and Information (Pty) Ltd* 2000 (3) SA 806 (C): 813- 4; *Symington v Pretoria-Oos Privaat Hospitaal Bedryfs (Pty) Ltd* 2005 5 SA 550 (SCA):562.

⁵⁰⁹ Mupangavanhu 2017:150-151; Esser and Du Plessis 2007:346.

⁵¹⁰ Esser and Du Plessis 2007:346.

⁵¹¹ Esser and Du Plessis 2007:346.

⁵¹² Esser and Du Plessis 2007:346.

⁵¹³ Delpont 2011:80. Lee 2005:68-69.

⁵¹⁴ A person elected or appointed to serve as the occasion requires, as a member of the board of a company in substitution for a particular elected or appointed director of that company.

⁵¹⁵ This would include de facto and de jure directors and pretended directors.

⁵¹⁶ Cassim et al 2018:236.

⁵¹⁷ Lee 2005:69.

are set out in sections 75-77 of the Act. In Australia, New Zealand and the United Kingdom,⁵¹⁸ Statutory statements of directors' duties replace the common-law duties of directors.⁵¹⁹

Different viewpoints regarding the legal relationship between a director and the company exist.⁵²⁰ Directors are a company's agents, trustees or managing partners.⁵²¹ In contrast to the Companies Act 61 of 1973, a director's powers were limited to the powers conferred onto him, and he did not have original powers to act as an agent. By acting as an agent, the director acts for the company's benefit.⁵²² Section 66 (1) of the Act considerably changed the director's position because it confers original powers and duties on the directors subject to the company's Memorandum of Incorporation. In certain circumstances, directors who act on behalf of the company are not liable unless they exceed their authority or expressly or implicitly assume liability.⁵²³

In terms of section 76⁵²⁴ of the Act, A director includes an alternate director, a prescribed officer⁵²⁵ or a member of a board committee or audit committee of a company, regardless of whether the individual is also a board member of the board of the company.⁵²⁶ Common law fiduciary duties include the duty to act in good faith, to act bona fide in the interests of the company and avoid a conflict between his/her own interests and the interests of the company.⁵²⁷

4.2 FIDUCIARY DUTIES

Originating from Roman-Dutch law, fiduciary duties are preventative in nature. Directors are obligated to act in the company's best interests and to be loyal to the organisation.⁵²⁸

⁵¹⁸ Section 170 (3) UK Companies Act 2006. Mupangavanhu 2017:151.

⁵¹⁹ Wiese 2018:67; Quinn 2014 58; Linnane 1996:298; Dbe 2003:281.

⁵²⁰ Lee 2005:69.

⁵²¹ Cassim et al 2018:240. McGregor 2011:399.

⁵²² Quinn 2014:58 made reference to the enlightened shareholder value model that requires directors to manage the company for the benefit of shareholders and non-shareholders. Fairfax 2008:2.

⁵²³ Thomas and Ferenczy 2002:9.

⁵²⁴ Sec 76 (1).

⁵²⁵ Sec 76 (1) (a).

⁵²⁶ Sec 76 (1) (b).

⁵²⁷ Mupangavanhu 2017:150-151.

⁵²⁸ Mupangavanhu 2017:157.

Mupangavanhu notes that :

*"[there] is a distinction between the common law fiduciary duty and duty of care, although these two duties are set out in section 76 (3) of the Act, the basis of liability for a breach of fiduciary duties is based on the general principle that a person standing in a fiduciary relationship with another commits a breach of trust if he or she acts for his or her own benefit or to the prejudice of the other person, a consequence of such a breach of trust can render the contract as voidable, or the director makes restitution to the company of either financial loss suffered by the company or for such financial benefit gained in breach of his duty."*⁵²⁹

In *Bristol and West Building Society v Mothew*,⁵³⁰ Lord Justice Millett, in the course of his judgment, defined a fiduciary:

*"[as] someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations."*⁵³¹

As confirmed in *Howard v Herrigel*,⁵³² no statute or common law makes a distinction between the fiduciary duties of executive and non-executive directors. It was held in *S v De Jager*⁵³³ the common law principle that directors must still act *bona fide* in the best interests of the company even if the directors had formally resigned as directors, they continued to be directors to fulfil their fiduciary duties, provided it is not in conflict with the

⁵²⁹ Mupangavanhu 2017:155-157.

⁵³⁰ *Mothew v. Bristol and West Building Society* [1996] EWCA Civ 533:8.

⁵³¹ *Mothew v. Bristol and West Building Society* [1996] EWCA Civ 533:8.

⁵³² *Howard v Herrigel* 1991 (2) SA 660 (A) 678.

⁵³³ *S v De Jager* 1965 (2) SA 616 (A).

current Act.⁵³⁴ According to Majmudar, directors are chosen by the board of directors and owe a fiduciary duty to shareholders and other stakeholders.⁵³⁵

4.3 DIRECTORS' DUTY OF CARE SKILL AND DILIGENCE

The duty of care, skill and diligence originates from English law.⁵³⁶ A dual objective-subjective test is adopted by South African courts when determining whether a director has breached his common law duty of care, skill and diligence.⁵³⁷ The duty of caring imposes a positive duty on a director to act with reasonable care and diligence in the best interests of the company.⁵³⁸ The standards of care and conduct apply equally to all directors.⁵³⁹ As stated by Mupangavanhu, Section 77 of the Act confirmed that the basis of liability for a breach of the duty of care, skill and diligence is a delict in the form of negligence.⁵⁴⁰

The nature of a director's duty of care, skill, and diligence is explained by Margo J in the *Fisheries Development Corporation of SA Ltd v Jorgensen*.⁵⁴¹

"To determine whether there was negligence in any of the conduct alleged, it is necessary to have regard to relevant aspects of a director's duty of care and skill. The extent of a director's duty of care and skill depends to a considerable degree on the nature of the company's business and on any particular obligation assumed by or assigned to him. In that regard there is a difference between the so-called full-time or executive director and the non-executive director... neither is required to have special business acumen or expertise, or singular ability or intelligence, or even experience in the business of the company. He is nevertheless expected to

⁵³⁴ Section 76 (3).

⁵³⁵ Majmudar 2021:76-77. According to Strine 2016:1247 "most European countries have corporate laws that expressly state that the corporation's managers have a duty to consider all the stakeholders of the corporation, not just stockholders, when managing the enterprise."

⁵³⁶ Mupangavanhu 2017:157.

⁵³⁷ Lee 2005:50.

⁵³⁸ Mupangavanhu 2017:158.

⁵³⁹ Mupangavanhu 2016:24; Du Plessis 2010:263.

⁵⁴⁰ Mupangavanhu 2017:158, Section 77 (2) stipulates that

"A director of a company may be held liable if

(b) in accordance with the principles of the common law relating to delict for any loss, damages or costs sustained by the company as a consequence of any breach by the director of-

(i) a duty contemplated in section 76 (3)(c)."

⁵⁴¹ *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 4 SA 156 W:165-168.

exercise the care which can reasonably be expected of a person with his knowledge and experience. A director is not liable for mere errors of judgment."

*Fisheries Development Corporation of SA Ltd v Jorgensen*⁵⁴² was, in turn, influenced by the English cases of *In re Brazilian Rubber Plantation and Estates Ltd*⁵⁴³ and *In re City Equitable Fire Insurance Co Ltd*.⁵⁴⁴ In *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company*,⁵⁴⁵ the court emphasized that if directors do not comply with the King Codes, this may result in a breach of duty to act with care, skill, and diligence.⁵⁴⁶ One of the crucial duties of a director is that of care and devotion in realizing the financial objectives of the organization and fulfilling future obligations to society.⁵⁴⁷ A director is expected to exercise reasonable care and is entitled to exercise his judgment after giving due consideration to information and advice from management unless there are proper reasons to question or specific grounds for suspicion.⁵⁴⁸

As explained by Du Plessis a director is not liable for mere errors of judgment. The required fault would be negligence measured against that of a reasonable person. A South African court must determine whether a director has breached his or her duty of care, skill, and diligence under common law.⁵⁴⁹ I agree with Lee⁵⁵⁰ that the terms of "care" and "skill" refer to different standards of liability and should not be used interchangeably. The standard of care required is an objective test, namely that to be expected of a reasonable man.⁵⁵¹

The duty of skill is a subjective test which refers to the duty of the individual to do his subjective best in particular circumstances, having regard to his own abilities and experience. The Act makes it mandatory for all directors to exercise their powers and perform their functions in good faith and for a proper purpose,⁵⁵² in the best interests of the company,⁵⁵³ with the degree of care, skill, and diligence that may reasonably be

⁵⁴² *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 4 SA 156 W:165.

⁵⁴³ *In re Brazilian Rubber Plantation and Estates Ltd* 1911 1 Ch 425; see also Du Plessis 2010:264.

⁵⁴⁴ *In re City Equitable Fire Insurance Co Ltd* 1925 1 Ch 407; see also Du Plessis 2010:264.

⁵⁴⁵ *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company Ltd* 2006 5 SA 333 (W)

⁵⁴⁶ *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 4 SA 156 W:165.

⁵⁴⁷ Majmudar 2021:76-79; Lee 2005:70.

⁵⁴⁸ Du Plessis 2010:265; Lee 2005:71-72.

⁵⁴⁹ Du Plessis 2010:286; Lee 2005:71.

⁵⁵⁰ Lee 2005:71.

⁵⁵¹ Lee 2005:71-73.

⁵⁵² Sec 76 (3) (a).

⁵⁵³ Sec 76 (3) (b).

expected of a person⁵⁵⁴ carrying out the same functions in relation to the company as those carried out by that director;⁵⁵⁵ and having general knowledge, skill and experience of that director.⁵⁵⁶

In section 77⁵⁵⁷ of the Act, a director can be held personally liable for losses incurred by the company due to his misconduct as a director.⁵⁵⁸ The Act⁵⁵⁹ does not introduce objective standards of care, skill, and diligence to determine if a director breaches his common law duty of care, skill, and diligence. As noted by Du Plessis, the fault that will be required is negligence as judged against the standards of a reasonable man with the director's skill, knowledge and experience.⁵⁶⁰

There are two different schools of thought on the issue of whose interests must be prioritized by directors when companies are managed. The first approach is the enlightened-shareholder-value approach, where the primary role of the directors is to manage the company to benefit the shareholders and ensure maximum value to the shareholders.⁵⁶¹ The second inclusive approach regards the interests of numerous stakeholders to be considered by directors on a case-by-case basis in the company's best interest.⁵⁶² Lee argues that in this era of increased corporate collapses due to poor corporate governance, there is a possibility of future courts applying a much stricter objective test, thereby holding directors liable for almost every decision or action that falls short of the reasonable man standard, irrespective of the individuals' competency, and impose stricter liability on company directors for breach of their common law duties of care, skill and diligence, when such a breach causes detriment to the company and its shareholders.⁵⁶³ Lee suggests that the codification of the business judgment rule will protect, provided certain conditions are met, company directors against the consequences of honest business mistakes.⁵⁶⁴

⁵⁵⁴ Sec 76 (3) (c); Majmudar 2021:76-78; Du Plessis 2010:263.

⁵⁵⁵ Sec 76 (3) (c) (i).

⁵⁵⁶ Sec 76 (3) (c) (ii).

⁵⁵⁷ Sec 76 (3) (a).

⁵⁵⁸ Barac et al 2010:21; Majmudar 2021:77; Lee 2005: 84. See Williams 2013:311-340 for a discussion of the liability of delinquent directors in the UK.

⁵⁵⁹ Sec 76 (3).

⁵⁶⁰ Du Plessis 2010:263; Lee 2005:70.

⁵⁶¹ Majmudar 2021:79

⁵⁶² Esser and Delpont 2017:101; Du Plessis 2010:263.

⁵⁶³ Lee 2005:50.

⁵⁶⁴ Lee 2005:50-51.

4.4. BUSINESS JUDGMENT RULE

The business judgment rule substantially prevents shareholders from holding directors accountable. The business judgment rule aims to protect the managerial power being exercised fully and freely by boards of directors.⁵⁶⁵ As stipulated in the Act,⁵⁶⁶ the business judgment rule requires that a director must act in the best interest of the company and stakeholders with the required care and skill.⁵⁶⁷ Section 218 (2) of the Act is drafted in wide terms⁵⁶⁸ and provides that "*any person⁵⁶⁹ who contravenes any provision of the Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention.*" Third parties can therefore argue that directors did not act in the best interest of the company⁵⁷⁰ and that liability for breach of duties and the duty of care and skill can be extended to third parties such as outside stakeholders.⁵⁷¹

Similar to USA, Australia and Germany, South Africa has codified the business judgment rule.⁵⁷² The business judgment rule adopted under section 76 (4) of the Act under "Standards of directors' conduct."⁵⁷³ The operation of the business judgment rule is two-fold. On the one hand, it promotes an interaction between a director's fiduciary duties to act in the best interest of the company and to avoid a conflict of interest of a financial nature under section 75 of the Act and on the other hand, the directors' duty of care skill and diligence.⁵⁷⁴

⁵⁶⁵ Bainbridge 2005:1747.

⁵⁶⁶ Sec 76 (3) (b)-(c).

⁵⁶⁷ Hippert 1997:18.

⁵⁶⁸ Esser and Delpont 2017:107.

⁵⁶⁹ This provision may deter experienced people to serve as directors.

⁵⁷⁰ As directed in Section 76 (3) (b) of the Act stakeholder will have to prove that by not acting in his/her best interest the director did not act in the best interest of the company

⁵⁷¹ Although no direct rights have been given to stakeholders.

⁵⁷² Mupangavanhu 2017:153-154 noted that other common-law jurisdictions such as UK and New Zealand have not codify the BJC into statute.

⁵⁷³ Mupangavanhu 2017:150 argues that it is incorrect to include the business judgment rule under standards of directors' conduct as a standard of conduct means how a director should conduct himself in fulfilling his duties as a director and exercising his discretion and powers. Mupangavanhu further explains the difference between the standard of review and standard of conduct becomes clear in cases where breach of a common law duty is alleged, the standard of review is the means to a review of the directors' conduct. The business judgment rule does not provide a standard of review as does the fiduciary duty or duty of care, skill and diligence.

⁵⁷⁴ Mupangavanhu 2017:150-163.

In 1982 Wiggings explained that the business judgment rule requires that a court can presume that the directors' business judgment is sound and not influenced by negligence, bad faith, self-interest, or abuse of discretion.⁵⁷⁵ In 1985 McMorris stated that the business judgment rule "immunizes management from potential liability when management acts within its and the corporation's authority, exercises due care, and complies with applicable fiduciary duties."⁵⁷⁶ He explained that the decisions of directors are presumed to be sound if it is made "in good faith and with a rational business purpose".⁵⁷⁷ Even if the decision leads to injury to the corporation and the shareholders, the director will be protected if it fulfils the requirement of good faith and a rational business purpose. He referred to the two basic assumptions that underlay this rule, namely that directors should not be held liable for bad business decisions and judgments where there is no abuse of discretion. The second assumption is because investors or shareholders can freely buy or sell their shares, they "voluntarily accepted the risk of poor management decisions."⁵⁷⁸

Walter noted that the doctrine of the business judgment rule was founded on the hypothesis that a corporate boardroom, and not a courtroom, is the most suitable setting for making business decisions.⁵⁷⁹ The rule attempts to balance the need of shareholders for a corrective mechanism against inefficient management against the business community's need to foster creative and risk-taking entrepreneurship. The rule represents the judiciary's reluctance to evaluate the merits of business transactions. Therefore, where the court has to determine if a board has acted in good faith and has exercised due care, the court will apply the rule and not evaluate the merits of the business decision.⁵⁸⁰

Davis explains the business judgment rule as "the proposition that corporate directors should not be faulted for an honest error of business judgment".⁵⁸¹ Walter emphasized that the legal presumption is that the rule shields a director from liability for losses incurred as a result of a mistake in judgment, albeit honest and reasoned.⁵⁸² Lee agrees with the

⁵⁷⁵ Wiggings 1982: 799.

⁵⁷⁶ McMorris 1985: 50.

⁵⁷⁷ McMorris 1985: 50.

⁵⁷⁸ McMorris 1985: 50.

⁵⁷⁹ Walter 1988:649-686. Jones 2007:327 is of the direct opposite opinion: "The fact that the business judgment rule was developed by the courts, and the fact that it blurs the distinction between the fiduciary duty and the duty of care and skill, demonstrate that American law on director's duties differs radically from South African law on this point."

⁵⁸⁰ Walter 1988:651; Lee 2005:50.

⁵⁸¹ Davis 2015:475.

⁵⁸² Walter 1988:649.

statement of Walter in that the rule, in effect, provides a "safe harbour" for directors and safeguards them from personal liability claims made against them because of errors of judgment or business decisions that have adversely affected the company.⁵⁸³

The business judgment rule is based on the legal determination that corporate directors, not judges, are best qualified to manage corporations.⁵⁸⁴ The business judgment rule was explained in *Cheff v Mathes*:⁵⁸⁵

*"[if] the directors satisfy their burden by showing good faith and reasonable investigation; the directors will not be penalized for an honest mistake of judgment, if the judgment appeared reasonable at the time the decision was made."*⁵⁸⁶

From a South African point of view, both Du Plessis⁵⁸⁷ and Cassim⁵⁸⁸ states that the business judgment rule is also referred to as a 'safe-harbour from liability' for directors that is very similar to the director's duty of care, skill and diligence.⁵⁸⁹ As explained by Cassim, section 76 (4) (a) of the Act incorporates a new business judgment rule that originates from American corporate law and is regarded as a cornerstone of corporate law.⁵⁹⁰ It has been implemented in Hong Kong and Australia but rejected in New Zealand and the United Kingdom.⁵⁹¹ The business judgment rule is a rule that prevents a court from interfering with the benefit of hindsight in honest and reasonable business decisions of the directors of the company.⁵⁹² Under the Act, the business judgment rule will have the balancing and practical effect of balancing the need of shareholders and stakeholders for a corrective

⁵⁸³ Walter 1988:651; Lee 2005:51; Du Plessis 2010:264; Davis 2015:476.

⁵⁸⁴ Walter 1988:650.

⁵⁸⁵ 199 A.2d 548, 555 (Del. 1964).

⁵⁸⁶ Walter 1988:650. *Cheff v. Mathes* 199 A.2d 548, 555 (Del. 1964). Ward 1978:244-245: "Nowhere, however, and certainly not in the view of our courts, are directors required to be superhuman or beyond mistake or insurers of damages which their companies may suffer. So long as they do what they believe to be in the best interest of the corporation and in their best judgment, the directors and officers are protected from liability to the corporation and its stockholders. This so-called business judgment rule, at least in my view, is an application of practical reason to corporate affairs. It is not practical for a court, and our courts have said essentially this, to rethink a business decision. The prospect of such second guessing would cause a kind of caution and self-protection in the board room which would be counterproductive to the efficiency of business."

⁵⁸⁷ Du Plessis 2010:264. Lee 2005:51-52.

⁵⁸⁸ Cassim 2018:310.

⁵⁸⁹ Du Plessis 2010:264. Lee 2005:51-52.

⁵⁹⁰ Cassim et al 2018:310-311.

⁵⁹¹ Cassim et al 2018:310. Bercea 2011:91 states it is the court's tendency not to censor business decisions taken in good faith and this creates the business judgment rule. Walter 1988:655.

⁵⁹² Cassim et al 2018:310-312. Walter 1988:653.

mechanism against inefficient management and alleviating the new and more rigorous duty of directors, members of a board, prescribed officers and audit committee, to exercise reasonable care skill and diligence in the performance of their duties.⁵⁹³

Du Plessis noted that a court would have to determine the following:

*"what the expected degree of care, skill and diligence is of a director 'carrying out the same functions in relation to the company as those carried out by that director whose conduct is being scrutinised and secondly, the court will also have to make a value judgment as to the degree of care, skill and experience that can be expected from such a director, with 'the general knowledge, skill and experience of that director whose conduct is scrutinised.'"*⁵⁹⁴

The requirements of section 76 (4) (a) of the Act for a director to be protected by the business judgment rule are that he or she must have taken reasonable diligent steps to make an informed decision about the matter,⁵⁹⁵ the director must have no personal financial interest in the subject matter of the decision and had no reasonable basis to know that a related person had a personal financial interest in the matter or alternatively must have made a proper disclosure to the board of directors of his or her interest or that of a related person.⁵⁹⁶ The director must have had a rational or reasonable basis for making or supporting the decision of a committee or the board with regard to that matter, and the director had a rational basis for believing and did believe that the decision was in the best interests of the company.⁵⁹⁷ As stated by Walter, the board's decisions must be informed, not simply a reliance on the expertise of financial advisors.⁵⁹⁸ Like Steinhoff's collapse in the Van Gorkom case, the directors were content with and relied on the CEO's presentations without informing themselves of the adequacy of a merger price and were deemed grossly negligent.⁵⁹⁹

⁵⁹³ Cassim et al 2018:310-311; Plessis 2010:264. Lee 2005:51-52; Walter 1988:649.

⁵⁹⁴ Du Plessis 2010:288; Walter 1988:649; Lee 2005:51-53.

⁵⁹⁵ Section 76 (4) (a) (i); Cassim et al 2018:311; Walter 1988:653.

⁵⁹⁶ Section 76 (4) (a) (ii) (aa)-(bb); Cassim et al 2018:311.

⁵⁹⁷ Section 76 (4) (a) (iii); Cassim et al 2018:311; Walter 1988:684.

⁵⁹⁸ Walter 1988:684-685.

⁵⁹⁹ Delport 2011:121; Walter 1988:684.

The test for reasonableness is objective, and the business judgment rule cannot apply if the business decision is unreasonable, fraudulent or dishonest. If the requirements of section 74(4)(a) of the Act are adhered to, a director will not be held liable for honest errors of judgment or reasonable mistakes that he or she may have made in the ordinary management of the company.⁶⁰⁰ The director will be regarded as having complied with his or her duty to act in the best interests of the company and the duty of reasonable care, skill and diligence. Fraudulent or dishonest business decisions are not protected.⁶⁰¹ If shareholders institute civil liability claims for damages based upon decisions that directors made, the courts will only examine the necessary extent to verify whether the requirements of the rule have been met and will not second-guess the merits of the decision.⁶⁰² The business judgment rule creates a presumption that the director acted on an informed basis in good faith⁶⁰³ and in the honest belief that the decision that was made was in the best interest of the company.⁶⁰⁴

The business judgment rule protects a director unless the presumption is rebutted. The burden lies on the party who challenges the decision to establish facts that will rebut the presumption.⁶⁰⁵ Directors may rely on expert advice to make informed decisions; however, as stated in the *HSCM Industries v ML SCM Acquisition* case,⁶⁰⁶ it remains the duty of directors to familiarize themselves with the information and be able to deliberate and question the experts' reports.⁶⁰⁷ If the party challenging the decision overcomes the presumption, the business judgment rule will not be applicable, and the courts will scrutinise the merits of the decision to determine whether there has been a breach of the directors' common law duty of care skill and diligence, which will result in personal liability.⁶⁰⁸ The business judgment rule co-exists with the common law duties of care, skill and diligence. It will not operate to protect directors who have breached their common law

⁶⁰⁰ Cassim et al 2018:310; Lee 2005:54; Mupangavanhu 2017:148.

⁶⁰¹ Cassim et al 2018:310-311.

⁶⁰² Lee 2005:54-55.

⁶⁰³ Kerr 2006:1051 noted that the duty to act in good faith: "is not a rule it is a general standard which includes compliance with the expectations of the parties involved and conforms to the spirit of the fiduciary relationship." Lee 2005:54-55.

⁶⁰⁴ Walter 1988:684; Kerr 2006:1051

⁶⁰⁵ Kerr 2006:1076.

⁶⁰⁶ Walter 1988:683. *HSCM Industries v ML SCM Acquisition Inc* 781 F.2d 264 (2nd Cir. 1986).

⁶⁰⁷ Walter 1988:681-684.

⁶⁰⁸ Kerr 2006:1051 noted that liability originates from an action and depends on when and where the duty of good faith is applied.

duties of care, skill and diligence from the consequences of negligent decisions.⁶⁰⁹ The business judgment rule will only protect directors against later challenges to their decisions that were properly made but have unfavourable consequences.⁶¹⁰

5. COMMITTEES

5.1 AUDIT COMMITTEE

The company must elect the audit committee and not the board of directors at each public company's annual general meeting. Regulation 42 of the Act requires that at any given time, a third of the audit committee members must have academic qualifications or experience in corporate governance, law, economics, public affairs, finance, commerce, human resource management, or accounting. The audit committee must comprise of a minimum of three directors who are not prescribed officers or involved in the daily management of the company or full-time executive employees of the company, inter-related company, or another related company.⁶¹¹ The rotation of auditors is compulsory.

5.2 SOCIAL AND ETHICS COMMITTEE

The Social and Ethics Committee ("SEC") is a company committee, not a board committee.⁶¹² It is a separate organ of the company and is appointed by the shareholders.⁶¹³ The SEC must consist of a minimum of three directors or prescribed officers. One⁶¹⁴ must be a director who is not involved in the daily management of the company's business or was so involved in the previous three years. The aims and functions of the social and ethics committee⁶¹⁵ are to act in the interest of shareholders and sensitise the board in respect of sustainable corporate social responsibility and the importance of the shareholders. It applies to all state-owned companies and public companies that are

⁶⁰⁹ Walter 1988:649; Kerr 2006:1051; McMorris 1985:59; see also Davis 2000:573-596.

⁶¹⁰ Lee 2005:55-56; Walter 1988:650; Kerr 2006:1038.

⁶¹¹ Delpont 2011:123.

⁶¹² If the SEC was a board committee the board could delegate additional power and authority to the SEC and annual reporting would only be to the board.

⁶¹³ Delpont 2011:88.

⁶¹⁴ Not a prescribed officer.

⁶¹⁵ Hereafter the SEC.

listed.⁶¹⁶ As alluded to by Jebe,⁶¹⁷ other functions include monitoring the company's activities regarding corruption, promoting equality, social and economic development, good corporate citizenship, consumer relations, contributions made to communities, public relations, and compliance with all relevant legislation and codes.⁶¹⁸

The SEC only has the powers and authority provided for in the Act and Regulations and is entitled to report annually to the shareholders at the company's annual general meeting.⁶¹⁹ Esser and Delpont⁶²⁰ argue that the precise mandate and scope of monitoring and reporting duties of the members of the SEC are not clear. The functions of the different committees may overlap. Two committees attending to the same matter may have different views and report to the board on the same issue.

6. STAKEHOLDER AND SHAREHOLDER INTERESTS

Corporate governance is also influenced by stakeholders such as staff, shareholders, clients, suppliers, creditors, and the government.⁶²¹ Shareholders (either themselves or via a proxy) are entitled to attend, speak and vote at a meeting. This provides a platform for shareholders to express their views, ask difficult questions to directors or lobby for support from other shareholders for a particular matter that needs to be decided. A shareholder may requisition a meeting by delivering signed demands to the company wherein the purpose for the meeting is specified. If the company regards the demands as frivolous, without merit or vexatious, it may apply to the court to set aside the demands.⁶²²

The board must defer to shareholders their approval either by ordinary resolutions⁶²³ or special resolutions⁶²⁴ on certain prescribed matters. As alluded to by Ogbodo,⁶²⁵ the corporate governance practice a company adopts is determined by the board of directors,

⁶¹⁶ Section 72 (4) of the Act.

⁶¹⁷ Jebe et al 2018:133.

⁶¹⁸ All relevant legislation and codes (especially King IV) are not listed in the Regulations.

⁶¹⁹ Jebe et al 2018:133.

⁶²⁰ Esser and Delpont 2017:228.

⁶²¹ Ogbodo et al 2018:137.

⁶²² Calkoen 2020:283.

⁶²³ The appointment or removal of a director and the entering into a Category 1 transaction under the listing requirements.

⁶²⁴ Amending the MOI or statutory mergers, disposal of all or majority of company's assets.

⁶²⁵ Ogbodo et al 2018:146.

whose legal responsibility is to create a system of checks and balances to monitor the performance and direction of the company and ensure long-term sustainability.

7. OTHER SOUTH AFRICAN CORPORATE SCANDALS

7.1 TONGAAT-HULETT SCANDAL

In March 2019, South Africa's largest sugar producer, Tongaat Hulett, appointed Pricewaterhouse Coopers (PwC)⁶²⁶ to investigate allegations of financial misconduct reported on their whistleblowing line. The 2018 financial statements were recalled, and a forensic investigation was pursued into alleged accounting irregularities, poor governance practices and the potential impact on the financial statements for the 2018 and 2019 financial years. The forensic investigation identified several existing internal policies, guidelines and frameworks that were applied incorrectly or ignored. The failure to adhere to governance guidelines, internal policies and frameworks created a culture of deference that resulted in employees following instructions on accounting practices without questioning those accounting practices. Against this background, senior executives were permitted to initiate or participate in financial reporting misstatements.⁶²⁷

In accordance with the PwC forensic investigation report (PwC report), civil claims to the value of R450 million will be instituted against previous directors and executives, and applications will be lodged to declare the involved directors delinquent.⁶²⁸ An auditor and six former company executives were charged with fraud.⁶²⁹ Logan⁶³⁰ observed that, similar to the Steinhoff scandal, substandard governance practices, lack of financial oversight and insufficient internal accountability resulted in a significant loss of value for shareholders

⁶²⁶ The same auditing firm that conducted the Steinhoff forensic investigation.

⁶²⁷ <https://www.biznews.com/sa-investing/2019/11/29/tonga-at-pwc-investigation-ex-senior-executives>
Accessed 17/07/2022.

⁶²⁸ <https://www.moneyweb.co.za/news/companies-and-deals/tonga-at-hulett-abandons-planned-r5bn-rights-offer/> Accessed 17/07/2022.

⁶²⁹ Allegedly falsifying the group's financial statements and backdating land sale agreements from the period March 2015 till September 2018.

⁶³⁰ Fund manager at Opportune Investments.

and stakeholders.⁶³¹ Like the Steinhoff scandal, the PwC report found that profits and asset values were substantially inflated, and executives created fictitious transactions.⁶³²

The PwC report was submitted to the board of Tongaat Hulett, and corrective measures were proposed.⁶³³ These corrective measures included developing a delegation authority framework, critical board committees, including the Social and Ethics committee, human resources and remuneration committee, and the risk committee that had to be established or reconstituted.⁶³⁴ In July 2022, the Johannesburg Stock Exchange (JSE) issued a public censure of Tongaat Hulett and financial penalties fine of R7.5 million for non-compliance with the JSE's listing requirements.⁶³⁵ It suspended it from trading on the JSE due to failure to publish provisional results timeously.⁶³⁶

But it did not end there. In June 2022, racketeering charges were added. In February 2023, the trial of six former Tongaat Hulett's executives started, but the trial was postponed till June 2023. The six include the former CEO, the former director for development planning, the legal executive and the finance executive, and an auditor from Deloitte Touche. The six are facing charges of racketeering pertaining to allegations of the manipulation of revenue sales of land by Tongaat Hulett's to the amount of R3.5bn.⁶³⁷

On 24 February 2023, Tongaat Hulett stated in a JSE regulatory notice that it had reached an agreement with Deloitte Touche to pay Tongaat Hulett R261 million in settlement of a claim for its role as auditor from 2012 to 2018.⁶³⁸ Among the governance failures identified

⁶³¹ <https://www.businessinsider.co.za/tonga-at-hulet-south-africa-financial-results-2018-pwc-investigation-2019-6> Accessed 19/07/2022.

⁶³² <https://www.biznews.com/thought-leaders/2019/06/19/tonga-at-hulett-sugary-case-maninjwa> Accessed 17/09/2022.

⁶³³ Njobeni 2019:1.

⁶³⁴ <https://www.businesslive.co.za/fm/features/2022-02-11-former-tonga-at-executives-appear-in-court-facing-19-fraud-charges/> Accessed 17/07/2022.

⁶³⁵ <https://cfo.co.za/articles/tonga-at-hulett-fined-r75-million-by-jse-for-noncompliance/> Accessed 20/07/2022.

⁶³⁶ <https://www.businesslive.co.za/bd/companies/industrials/2022-07-19-tonga-at-hulett-suspended-from-the-jse/> Accessed 20/07/2022.

⁶³⁷ <https://www.news24.com/fin24/companies/tonga-at-hulett-racketeering-charges-to-take-centre-stage-in-pre-trial-legal-battle-20230217> Accessed 17/2/2023

⁶³⁸ https://www.iol.co.za/business-report/companies/deloitte-to-pay-tonga-at-hulett-r261m-to-settle-accounting-claim-76b79674-12a4-485c-9f2a-2781f4d69b8a?utm_term=Autofeed&utm_medium=Social&utm_source=Facebook&fbclid=IwAR3VhUAeG2KJBr-bPc0jqMFvMHMidnRysVR9SQ7GJufcKu_JvqOyeBgQGqo#Echobox=1677219550 Accessed 2/26/2023

are the failure of Deloitte to report on profits from 2012 to 2018 being overstated and the overstatement of certain assets in Tongaat's financial statements.⁶³⁹ Deloitte did not investigate undesirable accounting practices that resulted in, among others, revenue being recognised in earlier reporting periods than it should have been and in expenses being inappropriately capitalised to assets.⁶⁴⁰ The practices led to an overstated R12 billion over seven years.⁶⁴¹

7.2 VBS BANK SCANDAL

In the VBS bank looting scandal, advocate Terry Motau was appointed⁶⁴² in terms of section 134 of the Financial Sector Regulation Act (hereafter the FSR Act) as an investigator⁶⁴³ to conduct an investigation and compile a report for the Prudential Authority. The investigative report was titled: The great heist.⁶⁴⁴ Included in its findings were that 2017 financial statements were fraudulent and misstated, banking systems were manipulated, and fictitious deposits were made.⁶⁴⁵ Substantial bribes were paid to numerous public officials to effect fictitious deposits to the majority stakeholder.⁶⁴⁶ Overdrawn banking facilities amounted to hundreds of millions of rand, leading to the widespread impoverishment of VBS depositors⁶⁴⁷. The auditor of VBS committed fraud in

⁶³⁹ https://www.iol.co.za/business-report/companies/deloitte-to-pay-tongaathulett-r261m-to-settle-accounting-claim-76b79674-12a4-485c-9f2a-2781f4d69b8a?utm_term=Autofeed&utm_medium=Social&utm_source=Facebook&fbclid=IwAR3VhUAeG2KJBr-bPc0jqMFvMHMidnRysVR9SQ7GJufcKu_JvqOyeBgQGqo#Echobox=1677219550
Accessed 2/26/2023

⁶⁴⁰ https://www.iol.co.za/business-report/companies/deloitte-to-pay-tongaathulett-r261m-to-settle-accounting-claim-76b79674-12a4-485c-9f2a-2781f4d69b8a?utm_term=Autofeed&utm_medium=Social&utm_source=Facebook&fbclid=IwAR3VhUAeG2KJBr-bPc0jqMFvMHMidnRysVR9SQ7GJufcKu_JvqOyeBgQGqo#Echobox=1677219550
Accessed 2/26/2023

⁶⁴¹ https://www.iol.co.za/business-report/companies/deloitte-to-pay-tongaathulett-r261m-to-settle-accounting-claim-76b79674-12a4-485c-9f2a-2781f4d69b8a?utm_term=Autofeed&utm_medium=Social&utm_source=Facebook&fbclid=IwAR3VhUAeG2KJBr-bPc0jqMFvMHMidnRysVR9SQ7GJufcKu_JvqOyeBgQGqo#Echobox=1677219550
Accessed 2/26/2023

⁶⁴² Appointed by the Deputy governor of the South African Reserve Bank and deputy CEO of the Prudential authority appointed in terms of Section 32 of the Financial Sector Regulation Act 9 of 2017.

⁶⁴³ Financial Sector Regulation Act

⁶⁴⁴ Motau 2018:3.

⁶⁴⁵ Motau 2018:23.

⁶⁴⁶ Vele Investments

⁶⁴⁷ Motau 2018:19.

signing off the banks' financial statements and regulatory reports when on 31 March 2017, the liabilities exceeded the assets by R180 million; thus, it was already insolvent.⁶⁴⁸

In March 2018, VBS was placed under curatorship. The report recommended that the persons who have been identified and involved in the looting of VBS bank, those who benefitted from the receipt or theft of funds and bribery, be criminally prosecuted.⁶⁴⁹ The financial officials and auditors responsible for creating fraudulent audited financial statements and reports should be criminally charged and prosecuted.⁶⁵⁰ The Prudential authority provides the report to the South African Revenue Services to institute criminal proceedings against the perpetrators for tax-related offences.⁶⁵¹ It is further recommended that the curator institute civil proceedings for the winding-up of VBS and final sequestration of those who benefitted from the bribery, theft and fraud. The asset forfeiture unit's intervention confiscates and preserves the crimes' proceeds.⁶⁵² National Treasury, curator, and the Prudential authority institute professional negligence claims against KPMG for the recovery of financial losses and report the auditors and attorneys involved in the scandal to their respective professional bodies to institute an action for professional negligence.⁶⁵³ It is evident from the report that financial reports need to be verified internally and externally by an independent auditor.⁶⁵⁴

7.3 GUPTA-OWNED COMPANIES

The Gupta family owned over 12 companies in South Africa. In 2017, a database leaked emails⁶⁵⁵ revealed how the Gupta family influenced South African state officials to obtain key contracts from state-owned enterprises. In the Estina dairy farm matter, R30 million was paid to the Guptas via the farm.⁶⁵⁶ The sole director of Estina was an IT salesman with

⁶⁴⁸ <https://www.news24.com/News24/explosive-report-into-vbs-bank-reveals-large-scale-looting>
Accessed 07/07/2022.

⁶⁴⁹ Motau 2018:137.

⁶⁵⁰ Motau 2018:136.

⁶⁵¹ Motau 2018:136-138.

⁶⁵² Motau 2018:138.

⁶⁵³ Motau 2018:139.

⁶⁵⁴ Du Plessis 2018:2.

⁶⁵⁵ A database of leaked emails between the Gupta family and key South African officials, which became known as the “#GuptaLeaks”.

⁶⁵⁶ The sole director of Estina was an IT salesman with no farming experience and used the same address as other Gupta companies.

No farming experience and used the same address as other Gupta companies. Financial records in the #GuptaLeaks indicated that over six weeks, R84 million was transferred at a time to the Gupta-controlled company.⁶⁵⁷

7.4 KPMG

In reaction to allegations that associated KPMG with the Gupta companies and the allegations of corruption at VBS, which KPMG audited, numerous companies left KPMG.

KPMG compiled a report that found that the South African Revenue Services had an apparent illegal fraud unit, and former finance minister Pravin Gordhan knew about it.⁶⁵⁸ KPMG International launched an investigation, and the report was withdrawn. The fees received from SARS were paid back to SARS, and the R40 million it earned from Gupta-related companies were donated to education and anti-corruption non-governmental organisations.

7.5 ESKOM

Allegations of irregular expenditure in the overpaying for the poor quality of coal linked to a contract from the Gupta own Tegeta mine and failure to adhere to internal company processes in the appointment of sub-contractors during the construction of the Kusile and Medupi power stations which are years behind schedule and billions of rands over budget. The financial irregularities at Eskom have caused national load-shedding that has had a severe negative effect on the economy.

7.6 BOSASA

⁶⁵⁷ <https://www.businessinsider.co.za/the-top-south-african-business-scandals-the-past-decade-2020-1>
Accessed 05/09/2022.

⁶⁵⁸ Named the “rogue spy unit” which was allegedly spying on former president Zuma.

African Global Operations, known as BOSASA, is accused of widespread corruption and bribing state officials to obtain state tenders. At the Zondo Commission, the former CEO and CFO testified how they had bribed officials.⁶⁵⁹

7.7 SASOL

An independent investigation into Sasol's Lake Charles Chemicals Project (LCCP) found inappropriate conduct and incompetence in the LCCP project management team. It also found that managers did not provide executives with accurate cost and schedule estimations. The joint CEOs agreed to resign.

7.8 PRASA

The failure of PRASA is the result of poor governance, bad leadership, theft and vandalism over more than a decade.⁶⁶⁰ In the latter part of 2019, PRASA cancelled all its irregular security contracts without a workable alternative to protect its railway network when the country went into lockdown because of the Covid-19 pandemic.⁶⁶¹ In December 2019, state-owned Prasa⁶⁶² was placed under administration. Repeat findings made by the auditor-general and public protector and ongoing investigations by the SIU⁶⁶³ into gross misconduct, irregular expenditure, fraudulent transactions, and corruption led to the pending suspension of senior officials.⁶⁶⁴

"The statistics are shocking: out of 590 stations, only 134 stations were functioning as the other 323 stations had been vandalised", Prasa's 2021/22 annual report reads. Of 40 lines, only 18 are operational and offer limited services, while more than 1 100km of signalling cable and 40km of rail tracks have been either stolen or damaged. The report did not

⁶⁵⁹ <https://www.businessinsider.co.za/the-top-south-african-business-scandals-the-past-decade-2020-1>
Accessed 05/09/2022.

⁶⁶⁰ <https://www.news24.com/fin24/companies/amabhungane-prasa-derails-critical-r75bn-train-repair-tender-20221213> accessed 13/3/2020.

⁶⁶¹ <https://www.news24.com/fin24/companies/amabhungane-prasa-derails-critical-r75bn-train-repair-tender-20221213> accessed 13/3/2020.

⁶⁶² Passenger rail agency of South Africa

⁶⁶³ Special investigating unit

⁶⁶⁴ <https://www.businesslive.co.za/bd/national/2020-03-13-prasa-suspends-12-on-gross-misconduct-allegations/> Accessed 13/3/2020.

mention the state of the remaining 133 stations.⁶⁶⁵ The passenger numbers have dropped, as shown by the 522 million passenger trips in 2011 and only 17 million in 2021.⁶⁶⁶

Another example of gross misconduct at PRASA is the complaint about the conduct of Judge Tintswalo Annah Nana Makhubele while she was chairperson of the interim board of PRASA.⁶⁶⁷ She is accused of gross misconduct due to her involvement in the so-called Siyaya matter. She allegedly circumvented PRASA's legal department to deal with a corruption-accused service provider.⁶⁶⁸ Siyaya tried to claim an R56-million settlement from PRASA despite objections by PRASA's legal department about the company's involvement in corruption at PRASA. Makhubele ignored this warning and paid the R56 million to Siyaya being seized from PRASA. The legal department had to bring an urgent application to the court to reverse the transaction.⁶⁶⁹

Furthermore, due to bad management, a wage agreement for 2021 was not honoured by PRASA. Even though under severe financial stress, it has been ordered by the Labour Court to pay employees a 5% increase which will raise Prasa's labour costs, which are already about R5.8 billion a year. In 2022 PRASA suffered R3.8 billion operational losses.⁶⁷⁰

8. CONCLUSION

In conclusion, corporate governance practices are the starting point for corporate and managerial accountability, productivity, responsibility and stakeholder protection.⁶⁷¹ The seven characteristics of good corporate governance are discipline, transparency, independence, accountability, responsibility, fairness and social responsibility.⁶⁷² If

⁶⁶⁵ <https://www.businesslive.co.za/bd/national/2020-03-13-prasa-suspends-12-on-gross-misconduct-allegations/> Accessed 13/3/2020.

⁶⁶⁶ <https://www.businesslive.co.za/bd/national/2020-03-13-prasa-suspends-12-on-gross-misconduct-allegations/> Accessed 13/3/2020.

⁶⁶⁷ <https://www.groundup.org.za/article/tribunal-against-ex-prasa-chair-judge-makhubele-set-for-next-week/> accessed 16/2/2023.

⁶⁶⁸ <https://www.groundup.org.za/article/tribunal-against-ex-prasa-chair-judge-makhubele-set-for-next-week/> accessed 16/2/2023.

⁶⁶⁹ <https://www.groundup.org.za/article/tribunal-against-ex-prasa-chair-judge-makhubele-set-for-next-week/> accessed 16/2/2023.

⁶⁷⁰ <https://www.news24.com/fin24/companies/prasa-to-cough-up-hundreds-of-millions-for-breaking-wage-agreement-20230202> accessed 16/2/2023

⁶⁷¹ Chauke and Sebola 2018:262.

⁶⁷² Lekhesa 2009:163-165.

companies do not adhere to these guidelines, they may encounter shareholder unhappiness and, subsequent to that, activism. There is the perception that good corporate governance principles positively affect the performance of a company and attract foreign investment.⁶⁷³ Financial scandals involve morally questionable financial behaviour, which has a negative widespread social impact on third parties⁶⁷⁴ and results in the loss of trust between shareholders and directors, which is detrimental to both parties.⁶⁷⁵

Good corporate governance principles have not significantly prevented dubious practices.⁶⁷⁶ Board independence is becoming a reality in South African companies, as 44% of all directors are now independent.⁶⁷⁷ However, the independence of directors in certain instances, as in the instance of Steinhoff, is questionable, as some independent directors might have established the companies or have served them for many years. In some instances, independence is just a title, as directors may not be independent in the true sense of the word.⁶⁷⁸

⁶⁷³ Munisi and Randøy 2013:93.

⁶⁷⁴ Toms 2019:478.

⁶⁷⁵ Wahla 2018:20.

⁶⁷⁶ Van Driel 2019:1271.

⁶⁷⁷ Cassim 2021 <https://www.unisa.ac.za/sites/corporate/default/News-&-Media/Articles/Flaws-in-South-Africas-approach-to-tenure-of-directors-of-companies> Accessed 31/05/2023.

⁶⁷⁸ Lekhesa 2009:163.

CHAPTER 5 STEINHOFF'S GOVERNANCE STRUCTURES AND PRACTICES

1. INTRODUCTION

This chapter will examine how the governance structure and practices in Steinhoff contributed to the collapse of Steinhoff. It will identify the corporate structures of Steinhoff before and after the collapse.

2. CHANGE TO TWO-TIER SYSTEM

In 2015 Steinhoff switched from a unitary to a two-tier board structure when its primary listing was moved from South Africa to Germany.⁶⁷⁹ The company has its statutory seat in the Netherlands and its head office in South Africa. It is registered with the trade register in Amsterdam and has its primary listing on the FSE in Germany. It has a secondary listing on the JSE in South Africa. The effect thereof was that the management board and supervisory board were independent of each other. The management board and supervisory board account to the general meeting. The corporate governance structure is based on the Articles,⁶⁸⁰ the regulations of the management board⁶⁸¹ and the regulations of the supervisory board and its committees, as well as the applicable laws and regulations, including the Dutch corporate governance code (refer to DCGC).⁶⁸² The DCGC has since been revised and approved in December 2022.⁶⁸³

Until 2015 Steinhoff had a primary listing on the JSE and was subjected to the King Code of Governance Principles of South Africa 2009 ("King III").⁶⁸⁴ Steinhoff is still listed on the

⁶⁷⁹ <https://www.mg.co.za/article/2018-01-2019-holes-in-Steinhoffs-management-led-to-corporate-scandal> Accessed 22/3/2018.

⁶⁸⁰ Articles of association of the Company as amended from time to time.

⁶⁸¹ The Regulations of the management board came into effect on 1 December 2015 and describe the powers, duties as well as working methods and the decision-making process of the management board. Certain significant resolutions of the management board are subject to the approval of the supervisory board and the general meeting.

⁶⁸² The Dutch corporate governance code www.mccg.nl Accessed 22/4/2020.

⁶⁸³ <https://www.mccg.nl/publicaties/codes/2022/12/20/dutch-corporate-governance-code-2022> Accessed 22/4/2023.

⁶⁸⁴ <https://www.businesslive.co.za/rdm/business/2018-06-18-the-steinhoff-saga-part-two-the-board-that-looked-the-other-way/> [tps://www.businesslive.co.za/rdm/business/2018-06-18-the-steinhoff-saga-part-two-the-board-that-looked-the-other-way](https://www.businesslive.co.za/rdm/business/2018-06-18-the-steinhoff-saga-part-two-the-board-that-looked-the-other-way/) Accessed 28/2/2021.

JSE. The question that arises is whether Steinhoff is complying with JSE listing requirements.⁶⁸⁵

In October 2020, JSE fined Steinhoff for breaching JSE listing requirements and publishing false, misleading and incorrect financial information. It was found that the reports did not meet international financial reporting standards. The JSE is still conducting an investigation into the conduct of management.⁶⁸⁶

On 2 November 2021, I sent an email to Steinhoff investor relations enquiring about whether Steinhoff has been exempted from any JSE listing requirements, and an email was received from Steinhoff investor relations stating:

*"[that] Steinhoff has a primary listing on the FSE, and a secondary listing on the JSE. As such Steinhoff needs to comply with the FSE listing requirements primarily. There are only a couple of JSE rules that apply".*⁶⁸⁷

I sent a follow-up email on 3 November 2021 requesting details about which JSE rules are applicable. However, no response was received.⁶⁸⁸

2.1 GERMAN TWO-TIER SYSTEM

The German legal system has two forms of corporations: the *Gesellschaft mit beschränkter Haftung*⁶⁸⁹ and the *Aktiengesellschaft*. The *Aktiengesellschaft* is a two-tier board system and consists of three organs a general meeting, a management board and a supervisory board.⁶⁹⁰

2.2 THE GENERAL MEETING

⁶⁸⁵ Paragraphs 7F5 to 7F6 of JSE listing requirements.

⁶⁸⁶ <https://cfo.co.za/articles/jse-fines-steinhoff-for-breaching-listing-requirements> Accessed 21/11/2021.

⁶⁸⁷ Copy of email on file with author.

⁶⁸⁸ Copy of email on file with author.

⁶⁸⁹ Du Plessis 1996:21.

⁶⁹⁰ Owen 2003:175.

The general meeting is excluded from managing and directing the company. It is the organ where the members or shareholders can enforce their rights. The management board can refer specific matters to the general meeting if a matter has been disapproved by the supervisory board. In so far as the institution of action is not regulated by other statutory provisions,⁶⁹¹ the general meeting can institute action against members of the supervisory board and management board.⁶⁹²

2.3 MANAGEMENT BOARD

The primary function of the management board is managing and directing the business of the corporation. The appointment of only natural persons and removal and remuneration of the members of the management board is determined by the supervisory board. No person can simultaneously be a management and supervisory board member.

2.3.1 DUTIES AND FUNCTIONS OF THE MANAGEMENT BOARD

The entire management board is required by law⁶⁹³ to manage the company as decent, reasonable and conscientious business leaders who are responsible for the direction and management of the company. In accordance with the Dutch corporate governance code ("DCGC"), a managing director is appointed for a maximum period of four years, and a managing director may be reappointed for a term of not more than four years at a time.⁶⁹⁴ On the proposal of the supervisory board, a managing director may be suspended or removed by the general meeting at any time. Managing directors may not be a member of the supervisory board or non-executive director of more than two listed companies. A managing director may not concurrently serve as a chairperson of a supervisory board or a one-tier board of a listed company.

2.3.2 LIABILITY AND INDEMNIFICATION

⁶⁹¹ Section 112 of the Aktiengesellschaft

⁶⁹² Du Plessis 1996:39.

⁶⁹³ Section 93(1) 1 of the Aktiengesellschaft

⁶⁹⁴ Steinhoff annual report 2017:85.

As Du Plessis⁶⁹⁵ emphasized, the members of the management board are regarded as “insiders” as they deal with insider documents of the company and may be held criminally liable for insider trading. Further, they must stand in good faith towards the company, and strict duties of care,⁶⁹⁶ skill and diligence are expected. A member (as a joint debtor) who is in breach of their statutory duties is liable for all damages to the company⁶⁹⁷ as well as criminal liability⁶⁹⁸ and will be removed from the board by the supervisory board.⁶⁹⁹ The burden of proof shifts to the member if there is any dispute about whether the member acted as a decent and conscientious leader.⁷⁰⁰ The burden of proof rests on the company to prove the nature and extent of the damage and the specific act which constituted the breach of duty, and the nexus between the act and the damage.⁷⁰¹

The civil and criminal potential of liability of the members of the management board is extraordinarily wide. However, in practice, instead of dragging out legal proceedings against members of the management board, these issues are normally resolved through the supervisory board’s control functions over the management board.⁷⁰²

2.4 SUPERVISORY BOARD

The general meeting appoints the supervisory board and consists of employees and independent, knowledgeable and experienced business people,⁷⁰³ thereby creating a voluntary discussion platform wherein the management board can consult with the supervisory board before making final decisions. The discussion platform enhances the advisory and monitoring function of the supervisory board and has the potential to influence corporate decisions indirectly.

⁶⁹⁵ Du Plessis 1996:36.

⁶⁹⁶ Du Plessis 1996:36 cautioned that these duties are not similar to the fiduciary duties known to the South African company law.

⁶⁹⁷ Section 93 (1) (2) of the Aktiengesellschaft.

⁶⁹⁸ Section 93 (2) of the Aktiengesellschaft.

⁶⁹⁹ Section 84 (3) of the Aktiengesellschaft.

⁷⁰⁰ Section 93 (1) (2) of the Aktiengesellschaft.

⁷⁰¹ Du Plessis 1996:36.

⁷⁰² Du Plessis 1996:38.

⁷⁰³ The members appointed by the general meeting are referred to as representatives of shareholders.

A management board member is not permitted to sit on the supervisory board of the same company.⁷⁰⁴ Du Plessis confirms the principal duty of the supervisory board is to supervise, appoint, and monitor the management board.⁷⁰⁵ The supervisory board is responsible for comparing and scrutinizing the financial statements it obtains from the management board. According to the *Aktiengesellschaft*,⁷⁰⁶ immediately after the financial statements have been audited, they must be presented by the management board to the supervisory board for approval and then considered validated. The supervisory board allows for consultation regarding policy decision and ensure that the management board acts lawfully and appropriately according to acceptable business practices.

According to Du Plessis:

"[the] problems relating to the supervisory board's effectiveness are because they do not act promptly and use their powers effectively. During a period of crisis, it is the responsibility of the supervisory board to intensify the supervisory control functions of the company, reallocate management duties, remove some (or all) members of the management board and appoint new members to the management board. It is not the duty of the management board to manage and direct the company. The supervisory functions of the supervisory board are parallel to the management functions of the management board." ⁷⁰⁷

The German legislature made provisions for various methods to ensure a free flow of information between the management board and the supervisory board relating to specific business matters as prescribed by the *Aktiengesellschaft* and within specific time frames. The supervisory board may request further information regarding specific matters at any time and convene a general meeting to discuss these matters. As stipulated in the *Aktiengesellschaft*,⁷⁰⁸ all members of the supervisory board (without any members such as the shareholder representatives being excluded) have an equal right to the obtained information.⁷⁰⁹

⁷⁰⁴ Du Plessis 1996:20.

⁷⁰⁵ Du Plessis 1996:29.

⁷⁰⁶ Section 172

⁷⁰⁷ Du Plessis 1996:28.

⁷⁰⁸ Section 90 (5)

⁷⁰⁹ Du Plessis 1996:30.

2.4.1 CHAIRPERSON OF THE SUPERVISORY BOARD

The chairperson of the supervisory board must, after receiving the requested information and no later than the first meeting after that, provide the supervisory board with the information. The chairperson is also responsible for the minutes of the meeting and regularly communicates with the management board.⁷¹⁰

2.4.2 DUTIES AND FUNCTIONS OF THE SUPERVISORY BOARD

The members of the supervisory board's conduct must meet the standards of a decent and conscientious business leader.⁷¹¹ The management board has exclusive management powers, and the supervisory board is prohibited by the statutory provision⁷¹² to manage and direct the business of the corporation, whereas the supervisory board is under a statutory duty to supervise or oversee the management of the corporation, these functions cannot be delegated. The functions of the supervisory board include the appointment and possible removal and remuneration of the members of the management board. The supervisory functions' nature and scope are not stereotyped and may vary according to the specific circumstances prevailing in a particular undertaking.⁷¹³

2.4.3 LIABILITY AND INDEMNIFICATION

As explained by Du Plessis,⁷¹⁴ similar to the rules applied to the members of the management board, the breach of duties may lead to criminal prosecution. The members of the supervisory board may also be held criminally liable for insider trading when they deal in defined insider documents. As stipulated in the *Aktiengesellschaft*⁷¹⁵ as a general rule and even without good cause and with a three-quarter majority, the general meeting may remove members of the supervisory board.

⁷¹⁰ Section 90 (5)

⁷¹¹ Section 116 and 93 (1) of the *Aktiengesellschaft*.

⁷¹² Section 76 (1) of the *Aktiengesellschaft*.

⁷¹³ Du Plessis 1996:34.

⁷¹⁴ Du Plessis 1996:33.

⁷¹⁵ Section 103 (1)

2.5 CONCLUDING REMARKS

The German two-tier system contains many checks and balances and, viewed in its entirety, has proven to be meaningful in Western Europe law, despite the existing difficulties between the duties and functions of members of the supervisory and management boards. The one-tier system is favoured in the United States and the United Kingdom.

The relationship between the supervisory and management board is complex. Steinhoff changed from a one-tier board system to a two-tier board structure which comprised a management board (consisting of three top executives) and a supervisory board (consisting of 9 non-executive directors). This change appears to have contributed to the management board not informing the supervisory board of decisions that were taken, and combined with Steinhoff's corporate culture being anchored by a dominant personality, it led to the supervisory board failing to fulfil its oversight role.⁷¹⁶ Amongst the most important principles of corporate governance are transparency and disclosure. The management board needs to provide all the information about the corporation regarding its financial results, objectives, salaries of senior management, the board members, and the structure and policies.⁷¹⁷

3. CORPORATE GOVERNANCE STRUCTURES OF STEINHOFF

3.1 EXECUTIVE COMMITTEE

The executive committee is appointed by the management board. During 2017 the members of the executive committee consisted of the CEO, COO, CFO, executive legal services, executive treasury and financing, executive deputy chairman KAP, finance executive, executive corporate services, group audit executive, chairman supervisory board, European retail market, Steinhoff Europe: Chief financial officer, Chief executive officer: UK retail, Executive: merger and acquisitions and group managing director at Pepkor.⁷¹⁸

⁷¹⁶ Skye 2018:3.

⁷¹⁷ Al Shunnaq and Al Azzam 2018:46.

⁷¹⁸ Steinhoff annual report 2017:85-87.

The executive committee was involved with assisting and advising the CEO in implementing strategies and policies determined by the management board in managing the business and affairs of the group. The executive committee monitored the performance of the group and assisted the CEO and CFO in preparing the annual budget for review and approval by the management board. The executive committee reviewed and monitored the company's risk management process. The executive committee consisted of 14 members (which included four directors).⁷¹⁹ No formal rules regarding the executive committee's working methods and decision-making process appear to have been established. After December 2017, the executive committee was dissolved.⁷²⁰

3.2 MANAGEMENT BOARD

The role of the management board, subject to the oversight of the supervisory board and guided by the company's interests, is to manage the company, achieve its strategy, and remain within its associated risk profile.⁷²¹ The management board and supervisory board are responsible for risk management and ensuring compliance with all applicable legislation and regulations.⁷²² The management board appoints the executive committee members and other committees to assist the management board in performing its duties. It establishes rules regarding its tasks, working methods and decision-making process.⁷²³ The management board may change the duties and composition of committees at any time.⁷²⁴

Per the Articles, the management board shall consist of at least two managing directors. The managing directors are nominated by the supervisory board and appointed by the general meeting.⁷²⁵ In accordance with the DCGC, a managing director is appointed for a maximum of four years and may be reappointed for a term of not more than four years at a time. A managing director may be suspended (on a proposal by the supervisory board)

⁷¹⁹ <https://www.biznews.com/global-investing/2018/01/30/steinhoff-board-structure> Accessed 23/6/2021.

⁷²⁰ Steinhoff annual report 2017:87.

⁷²¹ <https://www.mg.co.za/article/2018-01-2019-holes-in-Steinhoffs-management-led-to-corporate-scandal> Accessed 22/3/2018.

⁷²² Steinhoff annual report 2016:49.

⁷²³ Steinhoff annual report 2017:87.

⁷²⁴ Steinhoff annual report 2017:85.

⁷²⁵ Steinhoff annual report 2017:88.

by the general meeting. Steinhoff's management board in 2017 consisted of a CEO,⁷²⁶ COO⁷²⁷ and CFO.⁷²⁸

In terms of Principle 2.18⁷²⁹ paragraph 79⁷³⁰ of the Code, the board should conduct an independent assessment to determine whether a director's independence of character and judgment are affected or impaired by the service term of beyond nine years. With reference to a director's independence, I agree with Sharpe that cosmetic independence⁷³¹ should consider not only the director's corporate relationship with the company but also whether the director has the knowledge, time and information required for making critical decisions.⁷³²

During the 2017 reporting period, the management board comprised of Markus Jooste, CEO, Danie van der Merwe, COO and Ben la Grange, CFO. Jooste was appointed in 2000⁷³³ as CEO of Steinhoff Limited and chairman of Steinhoff Africa and in 2013 as CEO of Steinhoff Group's operation until December 2017, when he resigned. Jooste was also a director for 19 years, from September 1998 until December 2017. Jooste was appointed managing director from 2000 until May 2003. Jooste was a dominant executive, and fellow executives seldom questioned his actions or decisions.⁷³⁴ He previously served on the boards of various unlisted Steinhoff group companies and companies listed on the JSE and as a member of the remuneration committees of the following listed companies: PSG, Pepkor, Phumelela Gaming and Leisure Limited.

Bruno Steinhoff was director for almost 20 years, from September 1998 until February 2018.⁷³⁵ Christo Wiese was appointed director from March 2013 until May 2016 and

⁷²⁶ Chief executive officer

⁷²⁷ Chief operational officer

⁷²⁸ Chief financial officer

⁷²⁹ King III 2009:40.

⁷³⁰ Independent non-executive directors may serve longer than nine years if, after an independence assessment by the board, there are no relationships or circumstances likely to affect, or appearing to affect, the director's judgment. The assessment should show that the independent director's independence of character and judgment is not in any way affected or impaired by the length of service. A statement to this effect should be included in the integrated report.

⁷³¹ Cosmetic independence takes into account a director's relationship with the corporation.

⁷³² Sharpe 2011:1435.

⁷³³ Steinhoff annual report 2017:86.

⁷³⁴ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf>. Accessed 02/03/2021 25.

⁷³⁵ Steinhoff annual report 2016:37.

chairperson from May 2016 until 15 December 2017.⁷³⁶ Danie van der Merwe was a director for 19 years from 1999 until 2018 and COO from March 2013 until December 2017, and acting CEO from December 2018. Louis du Preez was appointed as CEO on 1 January 2019.⁷³⁷ Benjamin la Grange was appointed CFO on 30 November 2015 until January 2018, when he resigned as CFO and Managing Director of the company.⁷³⁸ None of the management board executives sat on the supervisory board. After December 2017, the executive committee was dissolved.⁷³⁹

Deenadayalen Konar was appointed chairperson from September 2008 until May 2016, when Christo Wiese replaced him.⁷⁴⁰ Konar was a director for 20 years, from September 1998 until Feb 2018. Claas Daun was a director for 20 years, from 1998 until 2018.⁷⁴¹ Stephan Grobler was a director from May 2009 until February 2018. Heather Sonn was a director from December 2013⁷⁴² until December 2017 and acting chairperson from 15 December 2017 until 20 April 2018. She was appointed chairperson on 20 April 2018. Steve Booysen has been a director for the past 11 years, from Sept 2009⁷⁴³ until present. Johan van Zyl was a director from May 2016⁷⁴⁴ until April 2018. Angela Krüger-Steinhoff has been a director since November 2015 till present.⁷⁴⁵ Dirk Schreiber was CFO of Steinhoff Europe from 2013 until December 2017. Siegmars Schmidt was the CFO of Steinhoff Europe from 1999 until 2013. Theodore de Klerk was appointed as CFO on 1 September 2019.⁷⁴⁶

At the date of the publication of the delayed Annual Report for 2017,⁷⁴⁷ the management board consisted of Louis du Preez, Philip Dieperink and Theodore de Klerk. It is not clear which criteria the board of Steinhoff⁷⁴⁸ used to classify its board members as independent and non-executive when for example, Markus Jooste, Steve Booysen, Len Konar Danie

⁷³⁶ Steinhoff annual report 2016:35.

⁷³⁷ <https://www.steinhoffinternational.com/leadership.php> Accessed 18/07/2021.

⁷³⁸ Styan 2018:121-122.

⁷³⁹ Steinhoff annual report 2017:87.

⁷⁴⁰ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> Accessed 02/03/2021. p25.

⁷⁴¹ Steinhoff annual report 2016:36.

⁷⁴² Steinhoff annual report 2016:37.

⁷⁴³ Steinhoff annual report 2016:36.

⁷⁴⁴ Steinhoff annual report 2016:37.

⁷⁴⁵ Steinhoff annual report 2016:37.

⁷⁴⁶ <https://www.steinhoffinternational.com/leadership.php> Accessed 18/07/2021.

⁷⁴⁷ Steinhoff annual report 2017:2.

⁷⁴⁸ Steinhoff annual report 2017:86-93.

van der Merwe, Siegmar Schmidt, Claas Daun⁷⁴⁹ and Bruno Steinhoff⁷⁵⁰ were directors for more than nine years. The entire management board is required by law to manage the company as decent, reasonable and conscientious business leaders who are responsible for the direction and management of the company. In accordance with the DCGC, a managing director is appointed for a maximum period of four years, and a managing director may be reappointed for a term of not more than four years at a time.⁷⁵¹ Steinhoff did not comply with the DCGC as managing directors served for more than four years and was reappointed for more than four years.

3.3 SUPERVISORY BOARD

The supervisory board of directors is responsible for corporate governance, determining the company's strategic direction, and supervising the company's management function to ensure the strategic plan is implemented. The supervisory board established the regulations and described the powers, duties, and decision-making process. The power of the board is restricted by section 66(1) of the Act or the company's MOI. The supervisory board accounts to the shareholders.

The primary duty of a director is to act in the best interest of the company.⁷⁵² It is mandatory for all directors to act in the best interests of the company.⁷⁵³ The Act does not differentiate between executive⁷⁵⁴ and non-executive directors.⁷⁵⁵ It defines a director as: "*a member of the board of a company or an alternate director of a company and includes any person occupying the position of a director or alternate director, by whatever name designated.*"⁷⁵⁶

The broadened definition of a director includes some senior company officials, even if a company official could be a designated manager, prescribed officers and members of the

⁷⁴⁹ Claas Daun was a director for 20 years from 1998 until 2018.

⁷⁵⁰ Bruno Steinhoff was director for almost 20 years from September 1998 until February 2018.

⁷⁵¹ DCGC Principle 2.2.1:27.

⁷⁵² Esser and Delpont 2017:98.

⁷⁵³ Sec 76 (3) (b).

⁷⁵⁴ Executive directors are full time executives/senior officials employed by the company and partake in the day-to day management of the company.

⁷⁵⁵ Non-executive directors are part time executives/senior officials who do not partake in the day-to day management of the company.

⁷⁵⁶ Sec 1.

board committee or the audit committee.⁷⁵⁷ The phrase “occupying the position of a director or alternate director” denotes a person who acts with or without lawful authority in the position of a director.⁷⁵⁸ The substance of the power exercised or functions performed is of greater importance in determining whether a person is a director.⁷⁵⁹ A director of a profit company⁷⁶⁰ must be elected by the shareholders for an indefinite term or a term as stipulated in the MOI.⁷⁶¹ Wiese⁷⁶² explains that⁷⁶³ different types of directors are categorized in terms of how they are appointed. Directors appointed in terms of the MOI⁷⁶⁴ are ex officio directors,⁷⁶⁵ alternate directors,⁷⁶⁶ elected directors,⁷⁶⁷ and temporary directors.⁷⁶⁸ Cassim⁷⁶⁹ remarked that the following types of directors are also recognized in our law, De jure director,⁷⁷⁰ nominee director,⁷⁷¹ puppet director,⁷⁷² de facto director⁷⁷³ and shadow director.⁷⁷⁴

As stated in the Steinhoff annual report of 2017,⁷⁷⁵ the 12 directors of the supervisory board (which included nine non-executive directors) were: Christo Wiese, chairperson;

⁷⁵⁷ Sec 77 (1)

⁷⁵⁸ Cassim et al 2018:236.

⁷⁵⁹ Mupangavanhu 2016:22.

⁷⁶⁰ Except the first director, a director appointed in terms of the MOI and an ex officio director.

⁷⁶¹ Cassim et al 2018:237.

⁷⁶² Wiese 2018:49.

⁷⁶³ Wiese 2018:49.

⁷⁶⁴ Memorandum of incorporation director is appointed or removed by any person who is named in the MOI.

⁷⁶⁵ Ex officio director is appointed as per the MOI of a company as a consequence of that person holding some other office, title, designation or similar status.

⁷⁶⁶ Alternate director as per the MOI of a company is appointed to serve as a substitution for another director for instance if a director is ill or has other commitments. The alternate director must exercise and discharge the same powers and duties of a director appointed to the company. Section 66 (4) (a) (iii).

⁷⁶⁷ Elected director is elected by a minimum of 50 per cent of the shareholders as per the MOI of a profit company and 50 per cent of the alternative directors. Section 66 (4) (b) of the Act

⁷⁶⁸ Temporary director is unless the MOI of the company states otherwise, temporarily appointed by the board to serve as a director of the company temporarily until the vacancy is filled.

⁷⁶⁹ Cassim et al 2018:238.

⁷⁷⁰ A de jure director is a person who has freely consented to being formally appointed as a company director.

⁷⁷¹ Nominee director is a person appointed by a major shareholder, class of shareholders, a significant creditor or an employee group to represent his or her interests. The nominee director is legally required to act in the best interests of the company and not the interests of any nominator, principal or employer.

⁷⁷² A puppet director is a person who is blindly following the instructions of his controller. He or she remains liable for breaching his or her fiduciary duties and cannot escape liability by laying the blame on his or her controller.

⁷⁷³ De facto director is a person who claims to act as a director without having been appointed validly or at all. He or she cannot escape liability because of not being formally or validly appointed as a director.

⁷⁷⁴ A shadow director is an anonymous director and has been recognised in our common law and continue to be a director for the purposes of his or her fiduciary duties.

⁷⁷⁵ Steinhoff annual report 2017:90.

Deenadayalen Konar, deputy chairman and independent director; Steve Booyen, supervisory director and independent non-executive director and head of the audit committee; Thierry Guibert supervisory director; and Theunie Lategan, independent non-executive director and supervisory director of the company, chairman of the human resources and remuneration committee and member of the audit and risk committee; Jayendra Naidoo, supervisory director; Angela Krüger-Steinhoff, supervisory director and a member of the nomination committee; Heather Sonn, supervisory director; Bruno Steinhoff, founder of the group and chairman of Steinhoff until the end of September 2008, and continued to serve as a non-executive director and assisting with special projects; Johan van Zyl, supervisory director; and Jacob Wiese, supervisory director.⁷⁷⁶

After April 2018, the following independent supervisory directors remained in office: Khanyisile Kweyama, Hugo Nelson, Alex Watson, Moira Moses and Peter Wakkie.

Munisi⁷⁷⁷ alludes that the allocated roles of the CEO and chairperson should be separate, and the monitoring board should comprise two-thirds of non-executive directors. The board of a company may appoint any number of committees of directors.⁷⁷⁸ It is unclear which criterion Steinhoff used to categorize executive directors as non-executive and independent for example, Franklin Sonn, Jannie Mouton, Deenadayalen Konar and Claas Daun were members of the board from 1999 and the independence of directors, Jannie Mouton and Christo Wiese with a significant cross-shareholding.⁷⁷⁹

In the Steinhoff annual reports of 2011⁷⁸⁰ and 2013,⁷⁸¹ almost similar statements were made regarding the independence and performance of non-executive board members serving more than nine years. As stated in the Steinhoff Annual Report of 2011:

"[that] the board has critically assessed and carefully considered the independence of Dr Len Konar, Dr Franklin Sonn, Mr Jannie Mouton and Mr Claas Daun, all of

⁷⁷⁶ Steinhoff annual report 2016:48.

⁷⁷⁷ Munisi and Randøy 2013:107.

⁷⁷⁸ Mitchell 2019:67.

⁷⁷⁹ <https://www.fin24.com/Opinion/the-steinhoff-saga-part-two-the-board-that-looked-the-other-way-20180628> Accessed 30/1/2019.

⁷⁸⁰ Steinhoff annual report 2011:84.

⁷⁸¹ Steinhoff annual report 2013:118.

*whom have served as independent non-executive directors for more than nine years, and has determined that each of these directors, who serve on other boards and have commitments and interests outside of the Steinhoff group, remains independent in character and judgment and that there are no relationships or circumstances which are likely to affect or which could appear to affect their judgment or independence of character and has determined that the length of service of these directors has not compromised, nor could be held to have compromised, their independence."*⁷⁸²

The fiduciary duties of care and loyalty require that a board of directors must acquaint themselves with all material information available before decisions are taken and in the honest belief that the action taken was in the best interest of the company.⁷⁸³ The Steinhoff management board did not keep the supervisory board informed, which resulted in failed oversight of the supervisory board for not raising red flags when the company was overtrading.⁷⁸⁴ The supervisory board had three standing committees, human resources and remuneration committee, nomination committee and audit and risk committee.⁷⁸⁵

4. STANDING COMMITTEES

4.1 HUMAN RESOURCES AND REMUNERATION COMMITTEE

As per Steinhoff's' annual report,⁷⁸⁶ the Human Resources and Remuneration Committee may not be chaired by the chairman of the supervisory board or by a former managing director or a supervisory director who is a member of the management board of another listed company. The above committee met twice a year and was responsible for not only drafting remuneration proposals for managing directors, senior managers and members of the executive committee but also the evaluation of the annual performance of the managing directors and supervisory directors, including the performance of a committee

⁷⁸² Steinhoff annual report 2011:84.

⁷⁸³ Grossman 2007:402.

⁷⁸⁴ <https://mg.co.za/article/2018-01-29-holes-in-steinhoffs-management-led-to-corporate-scandal/>
Accessed 30/07/2022.

⁷⁸⁵ Sec 66 (2) (b) states that an audit committee or a social and ethics committee as contemplated in section 72 (4) has to be established.

⁷⁸⁶ Steinhoff annual report 2017:94.

member and reporting the outcomes of the evaluations to the supervisory board. The committee also reviewed the unethical behaviour of senior managers and senior executives and reported on the outcomes of the evaluations to the supervisory board.⁷⁸⁷

The committee's tasks included the annual reviewing of the company's code of conduct and proposing amendments to the management board, drafting proposals to the supervisory board for the remuneration policy and remuneration of the managing directors and individual senior managers and members of the executive committee in the form of ordinary shares or rights to subscribe for ordinary shares. The committee was also tasked with the appointment of trustees and compliance officers with regard to the company's share-based incentive schemes and approval of the proposed amendments prior to consultation with the general meeting.⁷⁸⁸

Annually the committee assessed the functioning of the committee and reported the findings to the supervisory board. The committee supervised the policy of the management board on the selection criteria and appointment procedures for senior management other than managing directors who reported to the management board.

4.2 NOMINATION COMMITTEE

As stipulated in Steinhoff's Annual Report 2017,⁷⁸⁹ the nomination committee met annually. It was responsible for advising the supervisory board and drafting the selection criteria and appointment procedures for the supervisory directors and the managing directors. The nomination committee is also responsible for the annual evaluation and review of the board. Annually the committee assessed the functioning of individual supervisory directors and managing directors and the size and diverse composition (race, gender, skills and experience) of the supervisory board and management board and made proposals for the rotation of the supervisory board and the management board. I believe Steinhoff's nomination committee failed to assess the functioning of the different standing committees, considering the complexity of transactions and the composition of the

⁷⁸⁷ Steinhoff annual report 2017:94.

⁷⁸⁸ Steinhoff annual report 2017:94.

⁷⁸⁹ Steinhoff annual report 2017:94.

supervisory and management boards that comprised a majority of white males and not enough non-executive directors.

4.3 AUDIT AND RISK COMMITTEE

At each annual general meeting, the company⁷⁹⁰ must elect an audit committee. The main function of the audit and risk committee is to oversee the integrity and correctness of the company's financial statements and the relationship with external auditors.

The audit committee must consist of a chairperson and at least three directors (who are not involved in the day-to-day management of the company's business). The committee may not be chaired by the chairperson of the supervisory board or by a former managing director.⁷⁹¹ As stipulated in the Act,⁷⁹² the directors must not be material suppliers or customers of the company or be related to any of these persons in such a manner that a reasonable and informed third party would conclude in the circumstances that the integrity, impartiality or objectivity of any of these directors are compromised by that relationship.⁷⁹³

The audit committee is responsible for advising the supervisory board and supervising and monitoring the activities⁷⁹⁴ of the management board.⁷⁹⁵ The supervisory board establishes the audit committee's regulations, working methods, and decision-making process. The duties of the audit committee, as stipulated in the Act,⁷⁹⁶ are to nominate a registered auditor independent of the company and determine the remuneration fees and terms of engagement.⁷⁹⁷ A registered auditor must be appointed at each annual general meeting and is responsible for conducting an audit based on pre-determined audit criteria by following objective and systematic processes of collecting and evaluating evidence

⁷⁹⁰ Not the board of directors.

⁷⁹¹ Steinhoff annual report 2017:93.

⁷⁹² Section 94 (4).

⁷⁹³ Delpport 2011:123.

⁷⁹⁴ Operation of the internal risk management, audit department and control systems; The supervision of the enforcement of the applicable laws and codes of conduct; Compliance with recommendations and observations of internal audit department and external auditor; Provision of financial information; Compliance with Tax policy; If designated the role and functioning of the CFO; The independence and remuneration of the external auditor; The financing of the company; and The application of information and communication technology.

⁷⁹⁵ Steinhoff annual report 2017:93.

⁷⁹⁶ Section 90 (2) and any other legislation in relating to the appointment of auditors.

⁷⁹⁷ Section 94 (8).

concerning systems and information.⁷⁹⁸ The audit committee must state the services the auditor cannot perform⁷⁹⁹ and determines the nature and extent of any non-audit services that the auditor may provide to the company. It pre-approves any proposed contract for the provision of non-audit services.⁸⁰⁰

Regarding each financial year, the audit committee states in the financial statements whether it was satisfied that the auditor was independent of the company and comments on the financial statements, the accounting practices and internal financial controls of the company.⁸⁰¹ The audit committee attends to any internal and external complaints⁸⁰² and recommends to the supervisory board any matter relating to the company's accounting policies, financial control, records and reporting practices.

A public interest company must pay all expenses reasonably incurred by the audit committee, including the fees of any consultant or specialist engaged by the audit committee to assist in performing its duties.

Steinhoff's audit and risk committee had several weaknesses. The audit and risk committees were combined into one committee.⁸⁰³ In contrast with corporate governance guidelines, the audit and risk committees can be combined only if it can devote adequate time to their responsibilities. Only three members of the supervisory board sat on the committee, and five of the eleven supervisory board members served on the other committees. In considering the increased complexity of Steinhoff transactions, it is questionable whether the three members of the supervisory board could have devoted enough time to advising the supervisory board and supervising and monitoring the activities of the management board.⁸⁰⁴ The fact that a huge number of concluded transactions were undetected indicates that the risk and audit committee failed to perform

⁷⁹⁸ Visser et al 2010:25.

⁷⁹⁹ Section 93 (3).

⁸⁰⁰ Delpont 2011:123.

⁸⁰¹ Delpont 2011:124.

⁸⁰² Relating to accounting practices, the content or auditing of financial statements or any other related matters.

⁸⁰³ <https://www.mg.co.za/article/2018-01-2019-holes-in-Steinhoffs-management-led-to-its-corporate-scandal> Accessed 22/3/2018.

⁸⁰⁴ Steinhoff annual report 2017:93.

its duties effectively. On 25 June 2020, Steinhoff merged the governance, social and ethics committee into the audit and risk committee.⁸⁰⁵

4.4 GOVERNANCE AND SUSTAINABILITY COMMITTEE

This voluntary committee was established to assist the supervisory board, taking into account the relevant legislation, legal requirements and codes of best practice with the oversight and monitoring of social and ethical matters concerning social and economic development in terms of the goals and principles set out in the United Nations Global Compact Principles, the Organisation for Economic Co-operation and Development recommendations.⁸⁰⁶ Other duties included the monitoring of activities of the company relating to corporate social responsibility, thereby ensuring effective management, monitoring and reporting of the company's code of conduct.

4.5 SOCIAL AND ETHICS COMMITTEE

The Governance, Social and Ethics Committee (SEC) merged into the Audit and Risk Committee on 25 June 2020.⁸⁰⁷ As stipulated in section 66(2) (b) of the Act, the board may decide to either appoint an audit committee or a social and ethics committee as contemplated in section 72 (4) (a) of the Act. The Minister may prescribe, if it is in the public interest, by regulation, a category of companies that must have a social and ethics committee regarding the annual turnover,⁸⁰⁸ the workforce size⁸⁰⁹ or the nature and extent of the activities of such a company.⁸¹⁰ The functions⁸¹¹ and the rules governing the composition and conduct⁸¹² of the social and ethics committee are prescribed by the Minister. The SEC is a separate organ of the company.⁸¹³

⁸⁰⁵ <https://www.Steinhoff International Holdings NV | Leadership> Accessed 18/7/2021.

⁸⁰⁶ Steinhoff annual report 2017:95

⁸⁰⁷ <https://www.Steinhoff International Holdings NV | Leadership> Accessed 18/7/2021.

⁸⁰⁸ Section 72 (4) (a) (i).

⁸⁰⁹ Section 72 (4) (a) (ii).

⁸¹⁰ Section 72 (4) (a) (iii).

⁸¹¹ Section 72 (4) (b)

⁸¹² Section 72 (4) (c).

⁸¹³ Delpont 2011:88.

A company may apply to the Tribunal for exemption from that requirement.⁸¹⁴ This exemption may be granted if the company is required to have a formal mechanism within its structures that performs substantially the same functions as the social and ethics committee, and such a mechanism exists.⁸¹⁵ or it is not reasonable in the public interest to require the company to have a social and ethics committee given the nature and scope of the company's activities.⁸¹⁶ A granted exception is valid for five years or lesser periods as determined by the Tribunal, unless set aside by the Tribunal in accordance with subsection 7.⁸¹⁷The Companies and Intellectual Property Commission (CIPC) has the authority to apply to the Tribunal for the annulment of an exemption, either at its own discretion or upon the request of a shareholder or an individual granted standing by the Tribunal during the exemption application hearing. This application can only be made if it is determined that the grounds on which the exemption was originally granted are no longer applicable.⁸¹⁸ The SEC must have a minimum of three directors or prescribed officers. The SEC is responsible to report at the annual general meeting on the activities of companies in relation to social and economic development, as well as ensuring their adherence to principles of good corporate citizenship, including community contributions, donations, and charitable initiatives. Additionally, the SEC ensures that companies comply with consumer protection laws and labour regulations, promoting equality within their operations.⁸¹⁹

5. AUDITORS

The appointed auditor⁸²⁰ must be an independent registered auditor who has not been, at the time of appointment or for the previous five years, a company secretary, director, officer or employee of the company or of an entity that maintains the company's financial records or is related to such a person.⁸²¹ The appointed auditor may not serve as auditor or designated auditor for a period of five consecutive years.⁸²² It is prohibited for the same individual auditor to function in the capacity of auditor for more than five years in a row. If

⁸¹⁴ Section 72 (5).

⁸¹⁵ Section 72 (5) (a).

⁸¹⁶ Section 72 (5) (b).

⁸¹⁷ Section 72 (6).

⁸¹⁸ Section 72 (7).

⁸¹⁹ Delport 2011:89.

⁸²⁰ Either a person or firm.

⁸²¹ Section 90 (2) (b).

⁸²² Section 92.

he stops serving as an auditor or designated auditor of that firm after a term of less than five years, he is not eligible for appointment until at least two more financial years have passed.⁸²³

As stated by Butters, the auditing fees were exorbitant, raising concerns about the auditors' independence and objectivity.⁸²⁴ Despite the intra-group transactions between Steinhoff and Steinhoff Europe, the entire group was not audited by the same auditors. Steinhoff Europe was audited by another localised firm in Europe.⁸²⁵

6. COMPANY SECRETARY

Company secretaries are required by Section 86 of the Act for public and state-owned companies. The company secretary must oversee compliance with corporate law, rules, corporate governance, and the memorandum of incorporation and provide critical information to the board and management to make informed choices.⁸²⁶ Similar to the American corporate governance structures as contained in both the Delaware general corporations law⁸²⁷ and the Revised Model Business Corporation Act,⁸²⁸ the company secretary must ensure the preparation and attendance of meetings and that minutes of meetings held by shareholders, the board,⁸²⁹ any committees of the directors or the company's audit committee are properly recorded as stipulated in the Act.⁸³⁰

The company secretary is responsible to confirm and certify that the company complies with all the administrative requirements of the Act.⁸³¹ It is a requirement for every company to submit an annual return on a yearly basis, following the specified format, accompanied by the prescribed fee, and within the designated timeframe subsequent to the anniversary of its incorporation.⁸³²

⁸²³ Delpont 2011:121.

⁸²⁴ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> Accessed 02/03/2021. 24.

⁸²⁵ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> Accessed 02/03/2021. 25.

⁸²⁶ Armstrong 1998:97.

⁸²⁷ Section 142 (2) stipulates that the duty of one of the officers shall be to record the proceedings of stockholders and directors.

⁸²⁸ Section 8.4(c) stipulates that the by-laws or board of directors must assign an officer to prepare minutes of the directors' and shareholder's meetings, maintain and authenticate the records required to keep.

⁸²⁹ Owen 2003:173.

⁸³⁰ Section 88 (2) (d).

⁸³¹ Armstrong 1998:94.

⁸³² Section 33 (1).

In accordance with the Act, the company secretary may be designated to ensure compliance with the requirements of Section 33⁸³³ and ensure the highest levels of corporate governance compliance by national and international standards.⁸³⁴ The company secretary is aware of board discussions and the resolutions to authorize large-scale cash movements and is, therefore, the custodian of corporate governance, and it can well be asked what is the company secretaries' role in preventing unlawful transactions.⁸³⁵

6.1 DUTIES OF THE COMPANY SECRETARY

The appointment, duties and primary role of the company secretary are regulated by the Act⁸³⁶ and the JSE listing requirements. King IV provides guidelines as to the role and functions of the company secretary.⁸³⁷ The primary role is to advise and assist the board in fulfilling its corporate governance mandate. In terms of the Act,⁸³⁸ the appointed company secretary, while serving in that capacity, must be a permanent resident of the Republic of South Africa⁸³⁹ and is accountable to the board.⁸⁴⁰ The management board appoints and replaces the company's secretary subject to the approval of the Supervisory Board.⁸⁴¹ The company secretary acts as a secretary to the supervisory board's committees.

The company secretary's duties include but are not limited to guiding the directors individually and collectively as to their duties, responsibilities and powers.⁸⁴² The company secretary must inform directors of any law relevant to or affecting the company.⁸⁴³ The company secretary must also report to the board any failure on the part of the company or a director to comply with the Memorandum of Incorporation or rules of the company or the

⁸³³ Section 88 (2) (g).

⁸³⁴ Armstrong 1998:97.

⁸³⁵ <https://accountingacademy.co.za/news/read/steinhoff-where-was-the-company-secretary> Accessed 12/3/2019.

⁸³⁶ Section 86 (2).

⁸³⁷ Wiese 2018:34.

⁸³⁸ Section 86 (1).

⁸³⁹ Section 86 (2) (b).

⁸⁴⁰ Delpont 2011:120.

⁸⁴¹ Steinhoff Annual Report 2017:95

⁸⁴² Section 88 (2) (a).

⁸⁴³ Section 88 (2) (b).

Act.⁸⁴⁴ It is the responsibility of the company secretary to ensure that the minutes of all meetings involving shareholders, the board of directors, the audit committee, or any other committees of directors are accurately documented and in compliance with the Act.⁸⁴⁵ The company secretary must declare in the business's annual financial statements that the company has filed required Act returns and notices and that they are up to date, correct and truthful.⁸⁴⁶ A copy of the annual financial statements must be forwarded by the company secretary to everyone entitled to it.⁸⁴⁷

The directors' report in the financial statements must disclose if the board dismisses a company secretary.⁸⁴⁸ To increase transparency and inhibit boards from removing a company secretary whom they perceive to be meddlesome or a nuisance, for example, a company secretary who continuously highlights transgressions of the provisions of the Act or King IV or other legislation, the company secretary may require that a statement be included in its annual financial statements setting out the circumstances that resulted in such removal.⁸⁴⁹

As per the 2017 Steinhoff Annual Report, the company secretary was a legal entity, Steinhoff Secretarial Services Proprietary Limited, a South African registered company within the Steinhoff group⁸⁵⁰ and acted as a secretary to the supervisory board's committees. The company secretary must guide directors on their responsibilities, duties, and powers objectively and independently with care, skill, and diligence.⁸⁵¹ In the instance of Steinhoff, the question can be asked where was the company secretary when the annual and integrated reports of Steinhoff were evaluated and produced, only positive statements were made in the reports, and the impression was created of prosperous growth and enduring success. I agree with Esser and Delpont when seen with the benefit of hindsight, the genuine transparency of the published annual reports, as well as the absence of information between insiders and outsiders that was restricted to formal and audited

⁸⁴⁴ Section 88 (2) (c).

⁸⁴⁵ Section 88 (2) (d).

⁸⁴⁶ Section 88 (2) (e).

⁸⁴⁷ Section 88 (2) (f).

⁸⁴⁸ Section 89 (4).

⁸⁴⁹ Section 89 (2).

⁸⁵⁰ Steinhoff Annual Report 2017:88.

⁸⁵¹ Armstrong 1998:94.

statements, raised red lights regarding the ethical practises and foundation of Steinhoff's formed board.⁸⁵²

7. STAKEHOLDERS

The inclusive stakeholder approach posits that the board of directors should take into account the concerns and interests of all legitimate stakeholders, such as creditors and employees.⁸⁵³ The board must consider the interest of the stakeholders, including investors, employees, consumers and the general public, when managing the company.⁸⁵⁴ It is the responsibility of the social and ethics committee to afford protection to stakeholders in ensuring that directors fulfil their fiduciary duties.

Steinhoff's decisions had a devastating impact on our society, both economically and socially and therefore should act and be held responsible as corporate citizens.

8. SHAREHOLDERS

As emphasised by Chauke and Sebola, a director must act with honesty and integrity towards shareholders and must disclose any actual or potential conflicts of interest and guard against insider trading.⁸⁵⁵

Shareholders have a right to vote and share in dividends in return for their investment, but shareholders do not have a direct interest in the property, business or assets of a company.⁸⁵⁶ The main objective of companies is the maximisation of profits for their shareholders, as emphasized in *Mthimunye-Bakoro v Petroleum Oil and Gas Corporation of South Africa*⁸⁵⁷ and also the protection of the legitimate concerns of stakeholders and improve efficiency and performance and resource allocation.⁸⁵⁸ I am of the opinion that

⁸⁵² Wong 2009:2.

⁸⁵³ Esser and Delpont 2017:99.

⁸⁵⁴ Esser and Delpont 2017:104.

⁸⁵⁵ Chauke and Sebola 2018:262.

⁸⁵⁶ Chauke and Sebola 2018:258.

⁸⁵⁷ 2015 JOL 33744.

⁸⁵⁸ Esser and Delpont 2017:109.

with Steinhoff, the shareholders were not actively attending annual general meetings to become aware of the lack of oversight and transparency.

9. REGULATORY BODIES AND DISCLOSURES

The government establishes regulatory bodies and government agencies to ensure compliance with corporate governance and protect investors. These bodies include the Competition Commission, the Financial Sector Conduct Authority and the special commercial crimes unit. Butters alludes that in 2016 a high number of acquisitions were made by Steinhoff, for example, Steinhoff purchased the Home Retail Group, Poundland and Mattress Firm. These were complex transactions⁸⁶⁶ that made the comparability of Steinhoff's results difficult.⁸⁶⁷ Many transactions⁸⁶⁸ were concluded during the last day of Steinhoff's financial year.⁸⁶⁹ Butters mentions that the disclosures of business transactions were poor, the

⁸⁵⁹ Bainbridge 2005:1747.

⁸⁶⁰ Sec 76 (3) (b)-(c).

⁸⁶¹ Hippert 1997:18.

⁸⁶² Esser and Delpont 2017:107.

⁸⁶³ This provision may deter experienced people to serve as directors.

⁸⁶⁴ As directed in Section 76 (3) (b) of the Act stakeholder will have to proof that by not acting in his/her best interest the director did not act in the best interest of the company

⁸⁶⁵ Although no direct rights have been given to stakeholders.

⁸⁶⁶ A complex transaction can easily be structured in a way that could "manufacture" earnings for the group

⁸⁶⁷ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> accessed 02/03/2021. p26.

⁸⁶⁸ Hemisphere, JD Financial Services, Kika-Leiner, Mattress firm and Poundland

⁸⁶⁹ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> Accessed 02/03/2021. p26.

acquisition of ERM in 2008 was not announced via SENS⁸⁷⁰ and no cautionary announcement was made prior to the acquisition of Pepkor.⁸⁷¹

10. SHORTCOMINGS IN TERMS OF KING III AND IV ADHERENCE

With reference to Principle 1.3 of the King III code, the board should ensure that the company's ethics are managed effectively. It seems that the board's attempts to observe the Steinhoff code of ethics⁸⁷² and ensure that business practices are conducted subject to close scrutiny and beyond reproach have been ineffectual over the years. For example, in all the corporate governance reports between 2011⁸⁷³ and 2016, the same statement relating to Principle 1.3 is made:

*"[that] Steinhoff has not established a formal process of obtaining assurance on ethical awareness and ethical compliance throughout the group."*⁸⁷⁴

In King IV,⁸⁷⁵ a distinction is made between the executive⁸⁷⁶ and non-executive directors.⁸⁷⁷ The independent director is always a non-executive director⁸⁷⁸ who does not have a relationship with the company that could materially interfere with the objective and independent exercise of his or her judgment.⁸⁷⁹

As emphasized by Wiese,⁸⁸⁰ who refers to Principle 7 of the King IV report,⁸⁸¹ a director is considered not independent if he or she is:

- a) significant provider or ongoing funder or professional adviser to the company,

⁸⁷⁰ Stock Exchange New Service

⁸⁷¹ <https://www.prudential.co.za/media/31945/steinhoffs-red-flags.pdf> Accessed 02/03/2021. p27.

⁸⁷² Steinhoff Annual Report 2006:38.

⁸⁷³ Corporate governance report 2011:82.

⁸⁷⁴ Naude et al 2018:4.

⁸⁷⁵ King IV 2016:107.

⁸⁷⁶ Executive director is employed by the company and responsible for the management of the company.

⁸⁷⁷ Non-executive director is a part time director and not employed by the company and gives an independent and objective perspective on issues pertaining to the company. The non-executive director is required to maintain a broad knowledge of the financial and management aspects of the company.

⁸⁷⁸ Wiese 2018:50.

⁸⁷⁹ Cassim et al 2018:240.

⁸⁸⁰ Wiese 2018:50-51.

⁸⁸¹ King IV 2016:107.

- b) being a director who is also a shareholder and the holding is material to his or her personal wealth,
- c) being an ex-executive employee or auditor of the company during the preceding three years,
- d) being a person who participates in a share-based incentive scheme or is entitled to remuneration linked to the performance of the company,
- e) being a director or senior executive of a material supplier or customer.

As alluded to by Van Zyl and Mans-Kemp,⁸⁸² the King IV report does not provide guidance on the number of board positions that directors can be held concurrently, as multiple board positions might compromise their independence and create a conflict of interest.

Principle 2.18 of King III⁸⁸³ states that the board should comprise a balance of power, with a majority of independent, non-executive directors. Both independence of mind and the perceptions thereof are important,⁸⁸⁴ as confirmed in the King III report. Principle 2.18 paragraph 76⁸⁸⁵ states

"[that] independence should be assessed by weighing all relevant factors that may impair independence. The classification of directors in the integrated report, as independent or otherwise, should be done on the basis of this assessment."

And principle 2.18 paragraph 77 states

"any independent non-executive director serving more than nine years should be subjected to a rigorous review of his independence and performance by the board".⁸⁸⁶

As stated in King IV⁸⁸⁷ report, all entities must, by way of explanation, make a positive statement about how the principles have been applied and explain why it was not applied.

⁸⁸² Van Zyl and Mans-Kemp 2020:13.

⁸⁸³ King III 2009:37.

⁸⁸⁴ King III report 2009:38.

⁸⁸⁵ King III report 2009:40.

⁸⁸⁶ King III report 2009:40.

⁸⁸⁷ King IV report 2016:43.

The “apply and explain” approach requires more consideration and explanation by the governing body (board of directors) of what has actually been done to implement the principles and best practice recommendations of governance. As a result of this, stakeholders are enabled to determine better whether specific outcomes have been achieved.⁸⁸⁸

In the 2017 Annual Report,⁸⁸⁹ it is stated that Steinhoff International Holdings N.V. has its statutory seat in the Netherlands and its head office in South Africa. It is registered with the Trade Register in Amsterdam, the Netherlands, under number 63570173 and has its primary listing on the FSE in Germany. Steinhoff has a secondary listing on the JSE in South Africa⁸⁹⁰ and is required to comply with the 2008 DCGC, and as of 1 October 2017, the revised DCGC applies.⁸⁹¹ No reference to compliance in terms of the King IV report is made in any Steinhoff annual reports from 2017 until 2020. Neither the revised annual report of 2017 nor the annual reports of 2018, 2019 or 2020 are in compliance with the King IV report.

On 4 August 2021, I sent an email to Steinhoff International Holdings N.V. enquiring about the reason why no mention is made in the 2020 Annual report regarding compliance with the King IV Report.⁸⁹² On 11 August 2021, an email was received from Steinhoff International Holdings’ head of human resources stating that *“Steinhoff International is a Dutch company listed on the Frankford stock exchange which has to comply with the Dutch Code, the SA entity PEPKOR is fully compliant with the King IV.”*

11. CONCLUSION

Good corporate governance principles have not significantly prevented dubious practices⁸⁹³ but have the capacity to self-police. In terms of section 72 (4) of the Act, there should be a separate committee that attends to social and ethics. In the instance of Steinhoff, compliance with corporate governance would have been achieved if the

⁸⁸⁸ Van Zyl and Mans-Kemp 2020:4.

⁸⁸⁹ Steinhoff Annual Report 2017:85.

⁸⁹⁰ Steinhoff Annual Report 2017:97.

⁸⁹¹ Dutch corporate governance code.

⁸⁹² Copy of email on file with author.

⁸⁹³ Van Driel 2019:1271.

company had continuously developed an ethical framework and built an ethical base of directors, managers and staff members.⁸⁹⁴

When considering the independence of the board of Steinhoff, it becomes clear that the chairperson cannot be classified as independent when his personal interest was material to his wealth and contributing to this is the fact that his son also served on the board of Steinhoff. The delay in issuing the audited financial statements raised concerns about why the supervisory board did not timeously disclose nor address the risks and therefore failed in risk management.⁸⁹⁵ The question arises whether the board of directors fulfilled their fiduciary duties when the accounting irregularities, tax and criminal investigations in Germany raised international concerns, and they failed to address these issues. On 24 January 2022, the Cape Town High Court approved a R24 billion-rand settlement with investors.⁸⁹⁶

It is important to understand the differences between management and the context within which corporate governance systems are being implemented. Mere tick-box compliance with corporate governance principles does not prevent irregularities. However, the lack of proper corporate governance practices and principles contributed to the problems experienced at Steinhoff. Through various legislation, developing best practice guidelines and judicial decisions can influence and strengthen corporate governance systems.⁸⁹⁷

⁸⁹⁴ Chauke and Sebola 2018:262.

⁸⁹⁵ Al Shunnaq and Al Azzam 2018:46.

⁸⁹⁶ <https://www.businesslive.co.za/bd/companaies/retail-and-consumer/2022-01-24-court-gives-final-approval-to-r14bn-steinhoff-settlement> Accessed 25/01/2022.

⁸⁹⁷ Wong 2009:1.

CHAPTER 6: DISQUISITION OF DIFFERENT JURISDICTIONS

1. INTRODUCTION

*"The notorious collapse of Enron in 2001, one of America's largest companies, has focused international attention on company failures and the role that strong corporate governance needs to play to prevent them."*⁸⁹⁸

Global corporate failures in the 20th century led to the proliferation of international codes and laws to regulate and enhance corporate governance in their respective economies.⁸⁹⁹ The International Council on Global Governance Network (ICGN), Global governance principles, the United Nations (UN) Global Compact, and the Organisation for Economic Co-operation and Development (OECD) Corporate governance guidelines are examples of international codes.⁹⁰⁰

Corporate governance scandals in Europe resulted in each European Union (UN) member state implementing a national corporate governance code.⁹⁰¹ The United Nations' approach⁹⁰² to the enforcement of corporate governance codes is based on principles, in contrast to the United States' approach of mandating regulation.⁹⁰³ The principles-based approach was defined by Majmudar as the comply or explain paradigm, in which a corporation must justify why governance requirements were not met.⁹⁰⁴ The comply and explain approach is similar to South Africa's corporate governance system.

Cunningham explains that:

"[c]ommentators describe national models of corporate governance at a high level of generality for two reasons. First, a variety of corporate governance practices

⁸⁹⁸ Solomon 2007:11 quoted in Courthold 2010:55; <https://www.fin24.com/Opinion/the-steinhoff-saga-part-two-the-board-that-looked-the-other-way-20180628> Accessed 30/1/2019.

⁸⁹⁹ The British Maxwell companies, American Enron, European Parmalat, and South African Masterbond. China aviation oil in Singapore. Wiese 2018:4; Wade 2002:97; Anderson 2008:1082-1083; Roseme 2007:249.

⁹⁰⁰ Wiese 2018:5.

⁹⁰¹ Corporate scandals involving Parmalat and Royal Dutch Ahold were attributed to a variety of factors, including a lack of shareholder engagement, a lack of transparency and adequate supervision, the independence of non-executive directors, executive director compensation, and reporting failures.

⁹⁰² Also referred to as the "comply or explain" - basis approach.

⁹⁰³ Majmudar 2021:86.

⁹⁰⁴ Majmudar 2021:87.

*exists both within a particular country as well as across national borders. Second, the various legal systems that relate to corporate governance aim at protecting different interests, and they do so in diverse ways. A national model simply cannot incorporate all of these nuances. Therefore, it is always useful to encourage new conceptions of corporate governance that do not rely on a national model, but that instead transcend borders, whether international or intranational. To arrive at such a conception requires a new framework that distinguishes between the differing types of governance mechanisms that corporations use.*⁹⁰⁵

However, the effectiveness of corporate governance practices and systems is directly tied to the function that internal and external audits play in corporate governance, and both types of audits are essential components of the process. Hajduka provides a list of various corporate scandals that involve audit failures owing to the auditors. Some of these scandals are Maxwell and Polly Peck in Great Britain, Metallgesellschaft in Germany, Cedant, Waste Management, and Wirecard, which is currently being investigated for financial irregularities.⁹⁰⁶ In the United States, financial anomalies include qualified audit and Enron, which are analogous to Steinhoff's situation in South Africa.⁹⁰⁷

The corporate governance structures of the United States of America (USA), Germany and Australia will be identified and compared with the current corporate governance structures of South Africa. A detailed discussion of the different corporate governance structures is not within the scope of this thesis. The reasons for corporate governance failures and the preventative measures will be identified and compared with those of South Africa.

2. THE USA

2.1 INTRODUCTION

⁹⁰⁵ Majmudar 2021:87.

⁹⁰⁶ Hadjuka 2002:30; Fox 2002:868.

⁹⁰⁶ A top finance official at Wirecard was accused of engaging in a variety of financial irregularities in 2019, including the fabrication of accounts, laundering of money, and round-tripping in the company's Asia-Pacific operations. This led to the beginning of the collapse of Wirecard. <https://www.forbes.com/sites/forbesfinancecouncil/2020/07/27/three-early-lessons-from-the-wirecard-scandal/?sh=22e50c646bee/> Accessed 18/04/2023.

⁹⁰⁷ Hajduka 2002:30; Fox 2002:868.

The American corporate governance structure is a one-tier system (unitary board system), with officers, directors, and shareholders as participants.⁹⁰⁸ According to Owen, while state laws vary, *"the general default structure of corporate governance features certain predominant characteristics present in corporations of every state."*⁹⁰⁹ Employees play a peripheral role in the corporate governance model in the United States, while shareholders are the key participants.⁹¹⁰ Regulation, voluntary corporate governance regulations, and stock exchange rules govern corporate governance.⁹¹¹ By the end of 2002, numerous corporate scandals, which included investment scams, corporate malfeasance, unethical conduct and conflicts of interest, contributed to the collapse of WorldCom,⁹¹² Global Crossing,⁹¹³ Xerox,⁹¹⁴ Tyco⁹¹⁵ and Enron⁹¹⁶ and led to alarmed investors abandoning the public securities markets and the tumbling of U.S stock markets.⁹¹⁷

2.1.1 THE ENRON IMBROGLIO

According to Ronen and Gordon, Enron, a Houston-based energy trading and distribution company, announced on 16 October 2001 that it would reduce its after-tax net income by \$544 million and its stockholders' equity by \$1.2 billion due to accounting errors.⁹¹⁸ Enron was often called the "Darling of Wall Street",⁹¹⁹ and Fortune Magazine ranked it as the number one most innovative company in the USA.⁹²⁰ It was the seventh-largest U.S.

⁹⁰⁸ Owen 2003:171-173; Olson 2010:228; Moloney and Murphy 2013:141; Mitchell 2005:1314-1315; Mickels 2009:272-274.

⁹⁰⁹ Owen 2003:173.

⁹¹⁰ Clarke 2005:361. The global effect of the US corporate governance is having a clear influence on the Australian and UK corporate governance practices. Majmudar 2021:86 noted that in India the conflict is not between principals and agents as in the USA but a conflict between main shareholders and alternative shareholders. Kerr 2006:1081; Bebchuk 2006:1786.

⁹¹¹ Wiese 2018:207; Clarke 2005:365; Majmudar 2021:86.

⁹¹² Wallace 2003:103. WorldCom collapse involved accounting irregularities wherein earnings were inflated. Anderson 2008:1082 stated that The filing for bankruptcy by WorldCom was the most significant in the history of the United States. Grossman 2005:578; Hopt 2003:222-223; Ronen 2002:39-40; Eriksson 2003:191; Owen 2003:170; Fox 2002:868.

⁹¹³ Wallace 2003:102. The U.S. Securities and Exchange Commission investigated Global Crossing Ltd and its auditor Arthur Andersen for fraudulently inflated income, Global then applied for bankruptcy. Ronene 2002:40; Owen 2003:171; Fox 2002:868.

⁹¹⁴ Eriksson 2003:191; Ronen 2002:38-39.

⁹¹⁵ Wallace 2003:102. Tyco International was investigated for self-dealing by insiders and tax evasion. Eriksson 2003:191; Owen 2003:171.

⁹¹⁶ Murphy 2008:140; Wade 2002:97-104. Anderson 2008:1087; Grossman 2005:578; Owen 2003:169-170; Fox 2002: 868; Harris and Burns 2002:30-31.

⁹¹⁷ Anderson 2008:1082; Rochvarg 2003:89.

⁹¹⁸ Ronen 2002:38; Gordon 2002:1233; Peckron 2002:584.

⁹¹⁹ Ironically Steinhoff was often referred to as the "darling of investors". Thompson 2003:102.

⁹²⁰ Mmadu 2013:27; Mitchell 2005:1314.

corporation at the time of its collapse in November 2001.⁹²¹ On 2 December 2001, Enron filed for bankruptcy.⁹²²

Similar to Steinhoff, the financial collapse of Enron resulted in pandemonium, with hundreds of employees losing their jobs and retirement benefits.⁹²³ Shareholders and other parties incurred significant financial losses.⁹²⁴ Steinhoff's collapse was comparable to Enron's, allegedly due to non-compliance with accounting regulations, lack of oversight and gatekeeper failures of the board, and intricate financial schemes designed to defraud Enron's shareholders.⁹²⁵

Off-the-books partnerships, insider trading, offshore tax havens and the misuse of separate corporate entities covered various questionable activities, making the company appear to be more lucrative.⁹²⁶ Enron's stock plummeted, which resulted in huge job losses and loss of retirement savings.⁹²⁷ Both Enron and Andersen LLP (accounting firm) were prosecuted for reckless behaviour and accounting irregularities.⁹²⁸ The primary misdeeds of Enron and Steinhoff were questionable accounting decisions that created an image of phenomenal financial success.⁹²⁹

The Enron crisis led to a period of discussions and debates identifying the problems with corporate fraud, transparency, and the independence of major actors.⁹³⁰ The lessons learned from Enron related to unethical behaviour of attorneys, management and auditors,

⁹²¹ Thompson 2003:100; Uberoi 2018:2; Mmadu 2013:27. According to Anderson 2008:1082 in a period of less than 10 months Enron collapsed.

⁹²² Ronen 2002:38-39; Courthold 2010:55.

⁹²³ Thompson 2003:101; Wade 2002:98; Reece 2002:69; Rhode and Paton 2002:9-10.

⁹²⁴ Wade 2002:97; Kerr 2006:1080-1081. Rochvarg 2003:61 noted that the Enron scandal impacted on the regulation of the legal profession due to the misconduct of attorneys, corporate officials and accountants.

⁹²⁵ Thompson 2003:102. The corporate collapse of India's Satyam Computer Services is regarded as "India's Enron" wherein failure of transparency, accountability and lack of oversight of the board of directors of the company also resulted in accounting fraud and ultimately the collapse of India's leading software company. Uberoi 2018:3; Wallace 2003:96; Wade 2002:100. Kerr 2006:1081; Gordon 2002:1233; Courthold 2010:55. Owen 2003:169 noted that Enron misconstrued its financial situation it created special purpose entities ("SPE") to disguise debt and create the appearance of profitability and liquidity.

⁹²⁶ Thompson 2003:101; Wade 2002:98; Rhode and Paton 2002:9; Courthold 2010:55.

⁹²⁷ Thompson 2003:102; Kerr 2006:1081; Thomas and Ferenczy 2002:9. See Millom 2002:114-120.

⁹²⁸ Uberoi 2018:2; Wallace 2003:102. Arthur Andersen's conduct raised concerns about the lack of independency of auditing profession and the actual auditing process. Wade 2002:99.

⁹²⁹ Uberoi 2018:4; Wallace 2003:100; Wade 2002:100; Kerr 2006:1080-1082.

⁹³⁰ Wade 2002:99; Wallace 2003:91; Anderson 2008:1082; Rochvarg 2003:81.

ineffective financial disclosure, the management of pension funds, transparency, inattentive board oversight, and flaccid accounting practices.⁹³¹ Similar to Enron, the lessons learned from Steinhoff concerned ineffective board supervision, the composition of the board (the majority of board members were non-executive directors), and a lack of diversity. The structure of the audit committee was inadequate, the debt levels were out of control, and there was no transparent reporting. Unreliable information was disseminated to shareholders and stakeholders. The absence of an ethical committee reduced compliance with rules and regulations to a "tick-box" exercise.⁹³² As noted by Wallace, the fallout from Enron had "profound and lasting effects on corporate executives, accountants, attorneys, investors, securities analysts, stock exchanges, securities regulators, tax administrators, and transfer pricing specialists."⁹³³

The inadequacies and limitations of the current corporate governance system ultimately resulted in the reform of the American corporate governance system.⁹³⁴ Enron had become the new benchmark by which corporate collapses were measured.⁹³⁵ As emphasized by Hopt, the collapse of Enron sparked the largest federal criminal investigation and "trial of the century" of one company and led to the Sarbanes-Oxley Act.⁹³⁶

2.1.2 SARBANES-OXLEY ACT

In the United States, the response to the Enron affair was introducing a high level of regulation and prescriptive measures being put in place.⁹³⁷ These are contained in the Sarbanes-Oxley Act 2002 ("SOX").⁹³⁸ Known as the most comprehensive securities

⁹³¹ Wade 2002:97; Anderson 2008:1087; Hajduka 2002:30; Rochvarg 2003:89; Rhode and Paton 2002:9-10; Millon 2002:113.

⁹³² Naude et al 2018:2-7; Shu-Acquaye 2007:594.

⁹³³ Harris and Burns 2002:30.

⁹³⁴ Wallace 2003:120; Wade 2002:108; Hopt 2003:222.

⁹³⁵ Emshwiller 2011:3-4.

⁹³⁶ Hopt 2003:222-223; Emshwiller 2011:3-4.

⁹³⁷ Anonymous 2003:272; Woo2011:120.

⁹³⁸ Anonymous 2003:272.

legislation, the SOX⁹³⁹ was drafted by Senators Paul Sarbanes and Michael Oxley.⁹⁴⁰ On 20 July 2002, the United States Federal government implemented SOX.⁹⁴¹

Mmadu explains that the US Congress identified five major weaknesses which ultimately led to the enactment of the Sarbanes-Oxley Act of 2002 as “a remediable legislation against future corporate failures and to restore investors' confidence in the corporation business.” He emphasizes the major weakness of corporate governance; accounting and external audit functions; public disclosure systems; corporate ethics; and standards of conduct of key professionals in the capital markets.⁹⁴²

SOX introduces requirements for the certification of financial reports, and the chief executive officer and chief financial officer of all US and non-US companies must certify the contents of periodic reports filed under the Securities Exchange Act 1934.⁹⁴³ They must also give assurances regarding the effectiveness of internal controls.⁹⁴⁴ SOX introduces measures to improve audit regulation and includes a public company accounting oversight board to which all auditors of US public companies, as well as all non-US companies with US securities registrations, must register.⁹⁴⁵

The New York Stock Exchange (NYSE) adopted SOX, and all listed companies are required to comply with SOX.⁹⁴⁶ SOX identified gaps in the accounting practices of corporations and created a framework of regulatory prescriptions that compel public companies to improve internal controls and governance structures to protect the interests of shareholders and investors by improving accounting oversight, corporate disclosures, accurate and reliable financial disclosure and criminal fraud accountability.⁹⁴⁷ SOX

⁹³⁹ Sarbanes-Oxley Act 2002. Dbe 2003:282. Martella 2004:62-65. Thompson 2003:100-118. President Bush described SOX as “*the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt.*” <http://www.whitehouse.gov/news/releases/2002/07/200207> accessed 22/2/2023; Wade 2002:110; Kerr 2006:1081; Anderson 2008:1082.

⁹⁴⁰ Uberoi 2018:1-2; Wallace 2002:103-105.

⁹⁴¹ Krackhardt 2005:323; Clarke 2005:365; Kerr 2006:1081.

⁹⁴² Mmadu 2013:26-27.

⁹⁴³ Anonymous 2003:272.

⁹⁴⁴ Anonymous 2003:272.

⁹⁴⁵ Anonymous 2003:272; Mmadu 2013:28. Shu-Acquaye 2007:594 noted that the principal purpose of the oversight board is to protect the interests of investors and to engage public interest in the preparation of informative, accurate and independent audit reports.

⁹⁴⁶ Mloi 2008:36; Anderson 2008:1082.

⁹⁴⁷ Sharpe 2012:1. Uberoi 2018:2; Wallace 2003:104-106; Kerr 2006:1051, Bebchuk 2006:1785; Hopt 2003:222.

directed the Securities and Exchange Commission (hereafter "SEC") to promulgate such rules and regulations necessary to further SOX. The amendments to the American corporate governance system were far-reaching and significant.⁹⁴⁸ In terms of Section 303 of SOX, it is a criminal offence for directors of an organisation to mislead auditors.⁹⁴⁹ The state governs the compliance and enforcement of corporate governance standards, the dominant state law is that of Delaware, and many states have adopted the Model Business Corporation Act.⁹⁵⁰ All companies must act in accordance with the same set of mandatory rules. An advantage of the prescriptive mandatory approach is that it ensures transparency, enforceability and compliance with similar rules.⁹⁵¹ SOX confirms that corporate governance reforms are possible by implementing the right instrument, whether using a comply or explain-based code or strict regulation.⁹⁵² Hajduka favoured the general market theory⁹⁵³ and the prescriptive mandatory rules approach⁹⁵⁴ in light of the Enron collapse and the auditing failures.⁹⁵⁵

As alluded to by Uberoi, despite SOX being criticized as imposing significant costs, being rules-based, complex, inflexible and lacking a competitive edge.⁹⁵⁶ It is still beneficial for developing corporate governance norms and legislation in many developing countries such as Pakistan, India, and Bangladesh.⁹⁵⁷

Mmadu⁹⁵⁸ makes the following very critical statement:

"[T]hese post Enron self-regulatory reforms though commendable, came a bit too late and indeed, too little. The unhealthy scandals triggered a legislative revolution

⁹⁴⁸ Wallace 2003:104; Anderson 2008:1082-1083; Hannes 2013:294.

⁹⁴⁹ Moloi 2008:36. Similar to the Enron case wherein publicly reported financial results were falsified by chief executives and false and misleading public representations concerning Enron's business performance and financial condition were made. Wade 2002:97-102; Wallace 2003:104; Hopt 2003:221-222.

⁹⁵⁰ Ogbodo et al 2018:143.

⁹⁵¹ Sharpe 2012:38; Kerr 2006:1080.

⁹⁵² Wallace 2003:103; Wade 2002:108; Kerr 2006:1080.

⁹⁵³ Hajduka 2002:30-31. General market theory wherein market efficiency is interrelated with the concept of fairness and transparency in the market system.

⁹⁵⁴ Hajduka 2002:30 Prescriptive mandatory approach wherein the state influence and exercise control over market behaviour, efficiency and accounting regulations taking into account fairness, justice and equality for all in today's capital market system.

⁹⁵⁵ Hajduka 2002:30-31.

⁹⁵⁶ Eriksson 2003:182.

⁹⁵⁷ Uberoi 2018:2; Wallace 2003:103-105; Anderson 2008:1084.

⁹⁵⁸ Mmadu 2013:26.

*almost unheard of in American corporate history and resulted in a sea change in the corporate governance system in the United States. The general consensus of American Investors and majority of United States citizens was that corporate governance issues and auditor independence should not be left to the prevailing self-regulatory regime. Americans in the post Enron era were demanding heavy regulation of the corporate system."*⁹⁵⁹

The disadvantages of the rule-based approach are its inflexibility and applicability to all companies.⁹⁶⁰ In my opinion, however, the principle-based approach allows for flexibility in instances where a company, for a particular reason, chooses not to comply with a particular rule and has the opportunity to explain the reason for non-compliance.

2.2 BOARD COMPOSITION

The Anglo-American model of corporate governance relies on a single-tiered board of directors.⁹⁶¹ As expressed by Katarzyna, the governance form in America is a single-tier system wherein the company is governed by a unitary board alone that comprises of executive and non-executive directors.⁹⁶² As emphasized by Shu-Acquaye, the board of directors is the ultimate decision-making body of a corporation.⁹⁶³

Delaware provides for elections of directors at every annual meeting, and no provision is made for a fixed term for directors.⁹⁶⁴ The unitary board also represents the shareholders.⁹⁶⁵ The dominant participants in the one-tier system are officers, directors and shareholders.⁹⁶⁶ The ultimate responsibility rests with the board of directors to manage and supervise the performance of management and adhere to corporate governance

⁹⁵⁹ Mmadu 2013:26.

⁹⁶⁰ Krackhardt 2005:331. Clarke 2005:365; Shi 2007-200-203. Moss 2020:64-90.

⁹⁶¹ Unitary system. Clarke 2005:359. In Japan single tier system in contrast with the US single tier system focuses on the alignment of legal economic and social imperatives with the national system of corporate governance.

⁹⁶² Katarzyna 2016:67; Olson 2010:228.

⁹⁶³ Shu-Acquaye 2007:590-591.

⁹⁶⁴ Delaware General Corporation Law 2008 Section 141. Olson 2010:231 noted that the default rules for election of directors in Delaware and most US states is by plurality which in contrast to South Africa the default rule is by a majority of votes the Act section 68 (2).

⁹⁶⁵ Eriksson 2003:152. Delaware General Corporation Law 2008 Section 141

⁹⁶⁶ Owen 2003:171; Kerr 2006:1043.

measures.⁹⁶⁷ A director's powers to act on behalf of the corporation are derived from the state of incorporation.⁹⁶⁸ Sec 304 of SOX allows for the disgorgement of CFO and CEO compensation in the instance of restatement of financial statements.⁹⁶⁹ Insider loans and insider trading are prohibited.⁹⁷⁰ Employees are not forming a central part of corporate governance.⁹⁷¹

In Germany, employees are represented on the supervisory board and participate in supervising management; however, in Australia, there are no requirements for labour representation on the board.⁹⁷² Shi argues that employees are important stakeholders. It is good corporate governance practice to require employee representatives on the board of directors because they are involved with the day-to-day issues affecting the corporation, and the oversight over management would lead to employees having a voice in decision-making processes.⁹⁷³

The corporation laws in the United States⁹⁷⁴ provide more detailed requirements related to committee roles and functions. The Act, by contrast, contains no limitations on delegation to committees of the board, nor does it mandate independence of committee members

⁹⁶⁷ Wallace 2003:97; Kerr 2006:1066; Eriksson 2003:185. Horsey 1994:998 noted that a director must not only be acting in good faith but also in an informed manner.

⁹⁶⁸ Shu-Acquaye 2007:591 noted that the reason why fiduciary duties are used to describe the shareholder-manager relationship (The shareholder-manager relationship is characterized by the interaction between the owners of a corporation (the shareholders) and the individuals responsible for managing the corporation (the managers or executives). but not for other relationships such as creditor manager relationship (The creditor-manager relationship refers to the interaction between a company's creditors and the individuals responsible for managing the company's finances, the managers or executives).

⁹⁶⁹ Wallace 2003:104; see also Gage 2018:161-190 for a comprehensive discussion of the remuneration of directors in the USA.

⁹⁷⁰ Wallace 2003:104.

⁹⁷¹ Clarke 2005:361; Shi 2007-200-203.

⁹⁷² Shi 2007:208; Moss 2020:75; Wyburn 2010:65. Olson 2010:229 noted that the two tier board system distinguishes Germany from other major European models for example European Union companies may choose the European Company form *Societas Europaea* (SE) which provides for a unitary board. The SE was established by the European Union (EU) council in October 2001 and is subject to the EU rules on governance, accounting, and disclosure. It also provides for employee participation in the company's decision-making process, although the extent of this participation can vary depending on the national laws of the country in which the SE is registered.

⁹⁷³ Shi 2007:209.

⁹⁷⁴ Olson 2010:228 referred to the Delaware General Corporation Law 2008 Section 141 (c) (2) that specifically forbids a committee from approving or recommending any action to shareholders except for the election or removal of a director or amending the by-laws. Olson also referred to the Model Business Corporation Act 2002 Section 8.25 that forbids certain actions from being delegated to a committee such as filling a board vacancy, the independent approval of distributions or amending by-laws.

from managers. It expressly permits company managers to serve on committees *ex officio*.⁹⁷⁵

The United States differs from the United Kingdom in one critical aspect. In the United States, the CEO and chairperson of the board are not separated; often, it is the same individual acting as the CEO and chairperson of the board, whilst, in the United Kingdom, the CEO generally does not serve as chairperson of the board.⁹⁷⁶

2.2.1 FIDUCIARY DUTIES OF DIRECTORS

Historically the US courts did not burden corporate management with a fiduciary duty toward company shareholders and were not intended to exclude non-shareholders.⁹⁷⁷ The Delaware Supreme Court in *Guth v Loft*⁹⁷⁸ held that the standard of loyalty of directors is not measured on a fixed scale. Directors stand in a fiduciary relation of care, loyalty and fairness to the corporation and shareholders. The Guth rule is based on the principle that directors and corporate officers owe a fiduciary duty of loyalty to the corporation, which requires them to act in the best interests of the corporation and not their personal interests.⁹⁷⁹ This duty of loyalty includes the obligation to divulge any potential conflicts of interest and to refrain from using their position for personal gain. Provided directors act with due care, in good faith and with discretion, the courts that review their decisions will not second-guess its result.⁹⁸⁰ The fiduciary duties are used to prevent self-dealing, self-serving and criminal behaviour, such as embezzlement by directors and top management.⁹⁸¹

⁹⁷⁵ Olson 2010:228.

⁹⁷⁶ Ogbodo et al 2018 143; Owen 2003:173.

⁹⁷⁷ Radin 2007:383; Shu-Acquaye 2007:594 noted that these fiduciary duties and corporate governance have historically been viewed as a prerogative of the states and self-regulatory organizations

⁹⁷⁸ *Guth v Loft* 5 A.2d at 510, 510 (Del 1939).

⁹⁷⁹ The Guth rule, was established in the case *Guth v. Loft, Inc.* in 1939 by the Delaware Court of Chancery. Also known as the corporate opportunity doctrine, is a legal principle that governs the fiduciary duties of directors and corporate officers.

⁹⁸⁰ Animashaun 1989:348 mentioned the Guth-rule which states that a director or corporate officer is entirely free to engage in an independent, competitive business, provided he/she does not violate a legal or moral duty with respect to the fiduciary relationship between himself /herself and the corporation.

⁹⁸¹ Radin 2007:383.

A director's primary responsibility is to oversee the business of the corporation and to safeguard the well-being of the corporation.⁹⁸² Overseeing or monitoring functions of directors include to select, evaluate, fix the compensation of, and replacing senior executives.⁹⁸³ The board of directors should also monitor and evaluate the business of the corporation to ensure that the business is managed properly.⁹⁸⁴ Owen describes it as "*Whatever form the board takes, it continues to wield ultimate authority over, and responsibility for, decisions concerning the corporation.*"⁹⁸⁵

Feldman and Estra note that Delaware directors owe the corporation and its shareholders fiduciary duties even in insolvent circumstances and must exercise their business judgment in the best interest of the corporation and the benefit of the shareholders as owners.⁹⁸⁶

The Court stated that "An underlying premise for the imposition of fiduciary duties is a separation of legal control from beneficial ownership."⁹⁸⁷ According to Holland, with reference to the *Sutton* case,⁹⁸⁸ courts have consistently stated that directors of corporations are fiduciaries who must comply with the duties of care with reference to reasonable diligence and loyalty or fidelity.⁹⁸⁹ In Delaware, directors of corporations stand in a fiduciary relationship to the shareholders and to the corporations of which they are board members. According to Holland, the fiduciary responsibilities to both the corporation and its shareholders are triad, due care, loyalty, and good faith.⁹⁹⁰

According to Bisconti

"[t]he fiduciary duty of loyalty imposes on directors the obligation to consider and approve only those actions that he or she believes are in the best interest of the corporation. Self-dealing by a corporate director is the quintessential example of a

⁹⁸² Owen 2003:172. Animashaun 1989:347-349.

⁹⁸³ Owen 2003:172.

⁹⁸⁴ Owen 2003:172.

⁹⁸⁵ Owen 2003:172.

⁹⁸⁶ Feldman and Estra 2007:59.

⁹⁸⁷ *Malone v Brincat* 722 A.2d 5 (Del) 1998:9 quoted in Holland 2009:678.

⁹⁸⁸ *Charitable Corp. v. Sutton* 2 Atk. 400, 406, 26 Eng. Rep. 642 (Ch. 1742):645.

⁹⁸⁹ Holland 2009:678; McMurray 1987:605.

⁹⁹⁰ Holland 2009:681.

breach of the duty of loyalty. Self-dealing occurs when a director takes a personal benefit to the exclusion or detriment of the corporation and/or its shareholders."⁹⁹¹

According to Radin's theory of "stakeholder fiduciary duties, " directors and officers of corporations have a duty to consider all stakeholders' legitimate interests when making decisions that affect the corporations on whose boards they serve.⁹⁹² The observance of this duty is not absolute. It is not to prioritize stakeholder interests over shareholder interests but rather a duty to balance and reconcile the competing interests of all stakeholders to maximize long-term value for the corporation as a whole.⁹⁹³ Olson noted that in the USA, there are no rights of direct participation by stakeholders in corporate governance in contrast with Section 7 of the Act that promotes compliance with the Bill of Rights and reaffirms the concept of enhancing the economic welfare of South Africa as a partner within the global economy.⁹⁹⁴

For more than 120 years, derivative lawsuits have been part of the American judicial process. Derivative lawsuits are one of the most striking and threatening methods used by shareholders to monitor, exercise control over managers, and enforce anti-fraud rules and fiduciary duties in public corporations.⁹⁹⁵ Derivative lawsuits are unique to commercial law and comprise of two components. First, it is an action initiated by shareholders to compel the corporation to institute action. Secondly, it is an action by the corporation, asserted by the shareholders, against those liable to the corporation.⁹⁹⁶ Shareholders initiate derivative suits against the corporation by either a direct lawsuit or a derivative lawsuit. A direct lawsuit is an action wherein the shareholder individual attempts to claim damages for the violation of individual rights. Shareholders may also institute a class action for a claim of damages for violations of the corporation as an entity. Derivative actions are instituted by shareholders in instances where management, through fraud, neglect of duty or other causes, fails to take the necessary action to assert the rights of the corporation.⁹⁹⁷ As emphasized by Cooney, derivative actions include breach of fiduciary duties, waste of

⁹⁹¹ Bisconti 2009: 773; *Guth v Loft* 5 A.2d at 510 quoted in Animashaun 1989:346-348 that directors may treat a business opportunity as his/her own provided the opportunity is by nature not essential to the corporation and in which it has no interest or expectancy.

⁹⁹² Radin 2007:382-383.

⁹⁹³ Radin 2007:383.

⁹⁹⁴ Olson 2010:225.

⁹⁹⁵ Cooney 2003:717-718.

⁹⁹⁶ Cooney 2003:724.

⁹⁹⁷ Cooney 2003:719-720.

corporate assets, director or officer mismanagement, rescission of a sale of corporate assets and breach or enforcement of a contract between the corporation and a third party.⁹⁹⁸ While the derivative lawsuit is initiated by the shareholder, any recovery inures to the corporation and not the shareholder.⁹⁹⁹ Section 165 (2) of the Act provides that a derivative action may be instituted by employees through trade union representatives to recover financial losses.¹⁰⁰⁰

In the Steinhoff collapse, there are allegations that directors and officers had engaged in fraudulent accounting practices, which led to the inflation of the company's financial statements and the misrepresentation of the company's financial position. These allegations are similar to the reasons for the collapse of Enron and suggest that the company's directors and officers had breached their fiduciary duties to the company and its shareholders by failing to act in the best interests of the company and engaging in conduct that was harmful to the company its shareholders and stakeholders.

2.2.2 DIRECTORS' DUTIES OF CARE SKILL AND DILIGENCE

The general powers and duties of directors include the duty of care that requires a director to manage the business and affairs of the corporation with the level of care of a reasonable director in similar circumstances.¹⁰⁰¹ This means that a director will be in breach of this duty if he fails to manage the business and affairs of the corporation with this reasonable care.¹⁰⁰² This will include where a director fails to get the necessary information needed to take major corporate decisions.¹⁰⁰³ Horsey explains that the duty of care originated more than 200 years ago in the English common law of trust and the law of agency.¹⁰⁰⁴ During the 19th century in the USA, the concept of the fiduciary duty of care was limited to the directors of banks and other financial institutions. This was later extended to all directors.¹⁰⁰⁵

⁹⁹⁸ Cooney 2003:719.

⁹⁹⁹ Cooney 2003:719.

¹⁰⁰⁰ Olson 2010:224-225.

¹⁰⁰¹ Bisconti 2009: 774; Animashaun 1989:345.

¹⁰⁰² Bisconti 2009: 774.

¹⁰⁰³ Bisconti 2009: 774.

¹⁰⁰⁴ Horsey 1994:973.

¹⁰⁰⁵ Horsey 1994:973.

Adam and Matheson describe the duty of care as the circumstances where a director fulfil his duties in

*"[g]ood faith with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and in a manner he reasonably believes to be in the best interests of the corporation."*¹⁰⁰⁶

In *Smith v Van Gorkom*,¹⁰⁰⁷ the Delaware Supreme Court stated that the fiduciary duty of care requires from directors to exercise reasonable diligence, care and, in good faith, consider all relevant factors before making an informed business decision.

2.3 THE BUSINESS JUDGMENT RULE

2.3.1 INTRODUCTION

The development and application of the business judgment rule in the USA will first be discussed with reference to Delaware and Wisconsin. Thereafter a general discussion will follow.

2.3.2 DELAWARE AND WISCONSIN

According to Holland,¹⁰⁰⁸ the business judgment rule traces its origins to the 1742 decision of the Lord Chancellor in *Charitable Corp v Sutton*.¹⁰⁰⁹ With reference to Delaware corporate law, Holland states that *"the business judgment rule seeks to promote the full and free exercise of the statutory managerial power granted to Delaware directors while at the same time protecting the legitimate expectation of shareholder investors."*¹⁰¹⁰

In 1984, the Delaware Supreme Court refined the business judgment rule in *Aronson v Lewis*¹⁰¹¹ where the Court held that the business judgment rule *"is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in*

¹⁰⁰⁶ Adams and Matheson 2000:1108.

¹⁰⁰⁷ *Smith v Van Gorkom* (1985) 488 A2d 872-873.

¹⁰⁰⁸ Holland 2009:678.

¹⁰⁰⁹ *Charitable Corp v Sutton* 2 Atk. 400, 406, 26 Eng. Rep. 642 (Ch. 1742):645; Horsey 1994:973.

¹⁰¹⁰ Holland 2009:679.

¹⁰¹¹ *Aronson v Lewis* 473 A.2d 805 (Del) 1984.

good faith and in the honest belief that the action was taken in the best interests of the company."¹⁰¹²

The next year in *Smith v Van Gorkom*,¹⁰¹³ the Delaware Supreme Court referred to the main aim of the business judgment rule as

"[to] protect and promote the full and free exercise of the managerial power granted to directors."¹⁰¹⁴

The court held that directors could not rely on the business judgment rule based on decisions taken that were uninformed, unreasonable and irrational.¹⁰¹⁵ The court found several procedural errors and irregularities in the evaluation process and merger proposal that was submitted to shareholders for approval which amounted to gross negligence by the directors.¹⁰¹⁶ The court emphasized that no protection exists under the business judgment rule for unintelligent or unadvised decisions made by directors in a deliberate and informed manner.¹⁰¹⁷ In essence, the business judgment presumption includes a business decision taken in good faith with due care and without abuse of discretion in the legitimate furtherance of corporate purposes.¹⁰¹⁸

The Wisconsin courts¹⁰¹⁹ since 1900 also acknowledged the business judgment rule. In 1929 in *Polacheck v Michiwaukee Golf Club Land Co*,¹⁰²⁰ the court reiterated that "*courts will not interfere in the internal management of corporate affairs in the absence of allegations clearly disclosing abuse of power by corporate officers, bad faith or willful abuse*

¹⁰¹² *Aronson v Lewis* 473 A.2d 805 (Del) 1984:812 quoted in Holland 2009:681 and discussed in Goldman 1987:230-238.

¹⁰¹³ *Smith v Van Gorkom* (1985) 488 A2d 858 cited in Lee 2005:56-56 and cited in Goldman 1987:226; Walter 1988:684 and Animashaun 1989:349. See also Goldman 1987:230-238.

¹⁰¹⁴ *Smith v Van Cortom* 488 A.2d 858 (Del. 1985):872 quoted in Goldberg 1987:226.

¹⁰¹⁵ Lee 2005:56-56 illustrated the fact of how the court objectively considered whether the directors breached their duty of care. The court took into account that the directors after a mere two-hour meeting made the decision to sell the company, failed to read the proposed agreement thoroughly or enquire into the details of the agreed price. It was clear to the court that the decision was irrational unreasonable and uninformed. The court found the directors personally liable for any damages resulting from their decision to sell the company. Walter 1988:683; Animashaun 1989:345-346.

¹⁰¹⁶ Lee 2005:55; Wallace 2003:104; Walter 1988:685.

¹⁰¹⁷ Lee 2005:56; Walter 1988:684; Animashaun 1989:345-347.

¹⁰¹⁸ Animashaun 1989:363.

¹⁰¹⁹ Davis 2015:475 refers to the first two judgments in Wisconsin namely *Figge v Bergenthal* 130 Wis. 594 109 N.W. 581 (1907): 615, 624-25; *Theis v Durr*, 125 Wis. 651 104 N.W. 985 (1905): 659.

¹⁰²⁰ 198 Wis. 78 223 N.W. 233 (1929):82 quoted in Davis 2015:476-477.

of discretion or positive fraud."¹⁰²¹ However, in 2000 the Wisconsin courts described the business judgment rule as a judicially created doctrine in terms of which judicial review of directors' decisions is limited when the directors made it on an informed basis and in good faith with the honest belief that it would be in the best interest of the corporation.¹⁰²² The Wisconsin Court of Appeals added to this by stating that the business judgment rule limits judicial review of directors' decisions if a minimum level of care is exercised in the decision-making process.¹⁰²³

Unlike Delaware, it is clear that the Wisconsin courts will not add a duty of care requirement to the business judgment rule.¹⁰²⁴ Directors need to make sure that they get all the necessary information about the issue under consideration.¹⁰²⁵ This limitation (in comparison to the Delaware requirements) is based on the principle that judges should not substitute their own judgment for the judgment of the directors of the corporation because, in hindsight, it is possible to identify the questions the directors should have asked or which specific expert they should have contacted.¹⁰²⁶ It is also necessary to note that both Delaware and Wisconsin have kept the concept of the standard of conduct of directors apart from the standard of liability. This means that the responsibilities of directors can evolve without the fear of personal liability.¹⁰²⁷

2.3.3 DEFINITION AND APPLICATION

In 1829 in one of the cases adopting the business judgment rule, the court stated in *Percy v Millaudon*,¹⁰²⁸ "[t]he adoption of a course from which loss ensues cannot make the [director] responsible, if the error was one into which a prudent man might have fallen The test of responsibility therefore should be not the certainty of wisdom in others, but the possession of ordinary knowledge, and by showing that the error of the [director] is of so

¹⁰²¹ *Polacheck v Michiwaukee Golf Club Land Co* 198 Wis. 78 223 N.W. 233 (1929):82 quoted in Davis 2015:476-477.

¹⁰²² *Einhorn v Culea* 2000 WI 65, 235 Wis. 2d 646, 612 N.W.2d 78 cited by Davis 2015:481.

¹⁰²³ *Yates v. Holt-Smith*, 2009 WI App 79, 18-26, 319 Wis. 2d 756, 768 N.W.2d 213 cited by Davis 2015:481.

¹⁰²⁴ Davis 2015:482.

¹⁰²⁵ Davis 2015:482-483.

¹⁰²⁶ Davis 2015:482; Horsey 1994:972.

¹⁰²⁷ Davis 2015:486.

¹⁰²⁸ 10 Mart. 32 (La. 1829): 36-37 cited in Goldman 1987:226 footnote 3. Goldman 1987:226 footnote 3 also cited some of the other first cases adopting the business judgment rule: *Pollitz v Wabash Railroad* 207 N.Y. 113 124, 100 N.E. 721 (1912):724; *Hodges v New England Screw Co* 1 R.I. 312 (1850).

gross a kind that a man of common sense, and ordinary attention, would not have fallen into it."

Goldman describes the business judgment rule as a doctrine that was judicially created to prevent that qualified persons would refrain from serving as directors if the law requires a higher standard of care than would be required from an ordinary person in the performance of his duties.¹⁰²⁹ Goldman explains that the rule would allow "management to formulate policy and to make business decisions without the fear of personal liability."¹⁰³⁰ The business judgment rule protects the directors that acted in good faith and where the directors exercised sound business judgment.¹⁰³¹ In the circumstances, the rule prohibits judicial inquiry into the actions of the directors.¹⁰³² Basically, the business judgment rule protects directors from personal liability for losses suffered because of a mistake made in the performance of their duties performed in good faith and with sound business judgment.¹⁰³³ Goldman then states that a simple definition is that

*"[t]he business judgment rule is a presumption afforded to corporate directors in the exercise of corporate decision-making. The court presumes that in making a business decision, the directors acted on an informed basis, in good faith and in the honest belief that their actions were in the corporation's best interests."*¹⁰³⁴

Adams and Matheson summarize the business judgment rule as the circumstances where a director makes a business decision rationally and in good faith in an informed manner, and the director will be protected from further judicial scrutiny for reasonableness.¹⁰³⁵

Lee noted that in America, there is no statutory definition of the business judgment rule nor a common law definition.¹⁰³⁶ As alluded to by Mpangavanhu, the business judgment rule

¹⁰²⁹ Goldman 1987:225-226.

¹⁰³⁰ Goldman 1987:225-226.

¹⁰³¹ Animashaun 1989:363.

¹⁰³² Goldman 1987:225-226.

¹⁰³³ Goldman 1987:225-226.

¹⁰³⁴ Goldman 1987:227. Animashaun 1989:363 noted that the business judgment rule is a dynamic presumption necessary to balance business decisions made by directors with the fiduciary obligations of directors of protecting shareholders, stakeholders and companies from unlawful exercise of management decisions.

¹⁰³⁵ Adams and Matheson 2000:1108; Davis 2015:475.

¹⁰³⁶ Lee 2005:58-59 stated that in Australia the common law duties of company directors are codified in the Australian Companies Act (section 232 (4)) which states:"

developed as a common-law standard of review alongside the duty of care.¹⁰³⁷ In American corporate law, the platform for corporate governance is the fiduciary duties of directors which include the duty of care and the duty of loyalty.¹⁰³⁸ The business judgment rule arises in actions where parties seek to claim damages against directors for decisions that were taken.¹⁰³⁹ The courts will not question the merits of a decision taken by a director (as it assumes that the boardroom and not the courtroom is the most suitable forum for making business decisions). Still, they will examine the decision only to the extent necessary to verify whether the director acted with the necessary care that an ordinarily prudent person in a similar position and under the same circumstances would have taken.¹⁰⁴⁰ These duties are owned by shareholders and the company collectively. As stated by Lee:

*"[that] in essence, the duty of care requires a director to act with the care that an ordinary prudent person would be expected to exercise in a like position and under similar circumstances, while the duty of loyalty simply prohibits faithlessness and self-dealing."*¹⁰⁴¹

The business judgment rule creates a presumption that directors have acted in good faith, on an informed basis and in the honest belief that the decision taken was in the best interest of the company,¹⁰⁴² and it, therefore, protects directors from having to justify to shareholders or the courts the correctness of business decisions made in the ordinary management of the company.¹⁰⁴³ In the event of the presumption being refuted, the burden lies with the party who challenges the validity of the decision that was made, the business judgment rule will not be applicable, and the merits of the decision in question will be scrutinised by the courts to determine whether there has been a breach of the directors' common law duty of care.¹⁰⁴⁴

"that in the exercise of his or her powers and the discharge of his or her duties an officer of a corporation must exercise the degree of care and diligence that a reasonable person in a like position would exercise in that corporation's circumstances." The only other country is Ghana that has codified the common law duties of a company director.

¹⁰³⁷ Mpangavanhu 2017:152; see Bisconti 2009:774-778 for a discussion of the business judgment rule.

¹⁰³⁸ Lee 2005:53; Kerr 2006: 1080.

¹⁰³⁹ Lee 2005:52; Walter 1988:649, Mpangavanhu 2017:154.

¹⁰⁴⁰ Walter 1988:649. Kerr 2006:1080; Mpangavanhu 2017:153.

¹⁰⁴¹ Lee 2005:53.

¹⁰⁴² Walyer 1988:649; Kerr 2006:1081.

¹⁰⁴³ Walter 1988:650; Kerr 2006:1079; Bebchuk 2006:1784.

¹⁰⁴⁴ Lee 2005:52-53; Walter 1988:651.

The case of *Shlensky v Wrigley*¹⁰⁴⁵ is an example of the business judgment rule application in the USA.¹⁰⁴⁶ An action was brought by the minority shareholders against the board of directors for negligence and mismanagement for the decision not to install lights at the entrance of Wrigley Field, which resulted in low revenue for the baseball franchise.¹⁰⁴⁷ The court held that

*"it would not step in and interfere with honest business judgments of the directors unless there was a showing of fraud, illegality or conflict of interest."*¹⁰⁴⁸

After analysing the facts, the court held that the shareholder did not provide sufficient proof to rebut the presumptions of the business judgment rule in that the decision not to install lights was neither motivated by personal interests nor irrational.¹⁰⁴⁹ The directors successfully defended the matter.¹⁰⁵⁰ This is proof that traditionally the courts are reluctant to impede on decisions made by directors that were made in good faith based upon facts that they honestly and reasonably believed to have been in the best interest of the company.¹⁰⁵¹

Moreover, the fiduciary duty of care (which is a subjective enquiry) includes a director acting with the necessary care that an ordinary person in a similar position and under the same circumstances would be expected to act.¹⁰⁵² An example of where the court applied the fiduciary duty of care and imposed a stricter objective standard on company directors is in *Francis v United Jersey Bank*,¹⁰⁵³ wherein a senior director failed to prevent the misappropriation of funds. The court held that the director's failure to prevent the misappropriation of funds was a breach of the duty of care he owed to the company and its shareholders. The court noted:

¹⁰⁴⁵ *Shlensky v Wrigley* N.E. 2d 776 (Il. App. 1968). Cited by Lee 2005:54-56. *Cheff v Mathes* 199 A 2d 548, 555. Cited by Walter 1988:649.

¹⁰⁴⁶ Kerr 2006:1075-1076.

¹⁰⁴⁷ Lee 2005:55; Kerr 2006:1076; Mupangavanhu 2017:1536-156.

¹⁰⁴⁸ *Shlensky v Wrigley* N.E. 2d 776 (Il. App. 1968). Cited by Lee 2005:55.

¹⁰⁴⁹ Mupangavanhu 2017:153-154.

¹⁰⁵⁰ Mupangavanhu 2017:153-155.

¹⁰⁵¹ Lee 2005:55-56 noted that the reluctance of courts to interfere with decisions made by directors were illustrated in *Graham v Allis-Chalmers Manufacturing Co (1963) 41 Del Ch 78* wherein it was alleged that directors knew or had reason to believe that illegal price-fixing agreements were entered into by the senior executive, the court found that there was no evidence that the directors knew of such an arrangement or were negligent in appointing the senior executive. Walter 1988:649-685.

¹⁰⁵² Walter 1988:686; Kerr 2006:1079.

¹⁰⁵³ *Francis v United Jersey Bank* (1981) 432 A 2d cited by Lee 2005:54-56.

*"[that] A director is not an ornament but an essential component of the company... directors are under an obligation to keep informed about the activities of the company... when financial statements demonstrate that insiders are bleeding the corporation to death, a director should notice and try to stanch the flow of blood."*¹⁰⁵⁴

In *Cede v Technicolor*,¹⁰⁵⁵ the board of directors raised a defence that the decision to merge could not be scrutinised by the court as it met the requirements of the business judgment rule.¹⁰⁵⁶ The court found that the directors failed to meet the burden of proof to rebut the business judgment rule's presumptions.¹⁰⁵⁷ The court evaluated the substantive merits of the board's decision and found several failures which amounted to a breach of duty and care while determining whether each element of the business judgment rule had been met. Lee cautioned that:

*"the courts must not treat the business judgment rule as a substantive standard of conduct which entails some objective review of the quality of directors' decisions. The function of the business judgment rule is to set out certain elements that must be met in order for a court not to scrutinize the substantive merits of a director's decision."*¹⁰⁵⁸

2.3.4 CONCLUSION

To summarise: The business judgment rule requires that directors act i) with the necessary care that an ordinary prudent person in a similar position and under the same circumstances would have taken, ii) in good faith, iii) on an informed basis, iv) in the honest belief that their decision is in the best interest of the company, and v) with

¹⁰⁵⁴ Cited by Lee 2005:56.

¹⁰⁵⁵ *Cede & Co v Technicolor Inc* 634 A 2d 345 (Del 1993) as cited by Lee 2005:57; Kerr 2006:1077, Mupangavanhu 2017:154.

¹⁰⁵⁶ Lee 2005:57-58.

¹⁰⁵⁷ Lee 2005:57 noted that the court identified and considered the following failures which ultimately amounted to a breach of duty and care (1) the board was not adequately informed before approving the agreement, (2) the reasonable belief that once the merger was signed, no competing bids might have been made; (3) the board failed to make a prudent search for alternatives (4) the majority of directors had inadequate information about the terms of the merger before it was approved (5) the merger transaction was locked through stock options. Walter 1988:684. Kerr 2006:1076.

¹⁰⁵⁸ Lee 2005:58; Kerr 2006:1076-1080.

disinterestedness or no self-dealing by the directors. Measured against these requirements, the directors will not be held personally liable if the company suffers losses due to the actions or decisions of the directors.

2.4 AUDIT COMMITTEE

Martella¹⁰⁵⁹ and Olson¹⁰⁶⁰ illustrated the fact that audit committees play a critical and fundamental role in the company's financial reporting system. Therefore, it is required of audit committees to maintain an oversight of the internal accounting and controls of the company as well as take responsibility "*over the external audit function, adherence to regulatory, compliance and ethical mandates, and adequate communication involving management, the board of directors, the external auditors, and the company's shareholders.*"¹⁰⁶¹ In view of this, it is noted by Ericksson the functions of the audit committee have expanded significantly. It is directly responsible for the appointment, compensation and oversight of the work of the outside director. The auditing firm will report to the audit committee rather than the full board.¹⁰⁶² The audit committee's duties include the appointment of an auditing firm and monitoring the activities of management.¹⁰⁶³

The SOX further requires audit committees to establish procedures for the receipt, retention, and treatment of complaints received by the listed issuer regarding accounting, internal accounting controls, or auditing matters, as well as procedures for the confidential, anonymous submission by employees of the listed issuer of concerns regarding questionable accounting or auditing matters.

As alluded to by Wallace, audit committees are compulsory for listed companies.¹⁰⁶⁴ SOX¹⁰⁶⁵ requires that all audit committee members must be independent, and every five years, auditing firms must be rotated.¹⁰⁶⁶ The audit committee must comprise of one

¹⁰⁵⁹ Martella et al 2004:17.

¹⁰⁶⁰ Olson 2010:228-229.

¹⁰⁶¹ Martella et al 2004:62.

¹⁰⁶² Eriksson 2003:193.

¹⁰⁶³ Eriksson 2003:185-186; Eriksson 2003:193; Martella et al 2004:62.

¹⁰⁶⁴ Wallace 2003:104. Section 407 of SOX; Eriksson:186.

¹⁰⁶⁵ Section 301.Wallace 2003:106.

¹⁰⁶⁶ Wallace 2003:105.

financial expert,¹⁰⁶⁷ and members must be involved in corporate operations.¹⁰⁶⁸ The financial expert's main responsibility is to ensure transparency, detect irregularities timeously and ensure the integrity of the financial reports.¹⁰⁶⁹ A public company accounting oversight board ("PCAOB") was created to oversee public company auditing.¹⁰⁷⁰

The audit committee can also engage independent counsel and other advisers as necessary for the audit committee to fulfil its duties.¹⁰⁷¹ The audit committee is also responsible to determine the payment of compensation to any registered public accounting firm responsible for preparing or issuing an audit report or performing other audit, review or attest services, as well as payment of compensation to advisers employed by the audit committee.¹⁰⁷² The audit committee is also responsible for determining the payment of administrative expenses of the audit committee needed to carry out its functions.¹⁰⁷³

2.5 REPORTING AND DISCLOSURE

Harris and Burns emphasize that the Enron collapse refocused the attention on accounting standards and especially that transparency must be a key consideration for all parties involved in the corporation.¹⁰⁷⁴ Bartholmeusz explains the importance of disclosure to the public with an emphasis on the protection of investors and creditors through disclosure of sufficient information, of sufficient integrity and with sufficient timeliness, in order for them to protect themselves from either dishonesty or recklessness.¹⁰⁷⁵ Bartholmeusz is of the opinion that the legal framework governing corporate behaviour and regulating securities markets must protect investors and creditors from dishonest behaviour by boards, management and other participants through sufficient disclosure.¹⁰⁷⁶ However, US legislation pertaining to disclosure promotes transparency of the performance of the

¹⁰⁶⁷ Section 407 of SOX requires company disclosure regarding the expert. Wallace 2003:104.

¹⁰⁶⁸ Gordon 2021:1; Shi 2007-197-203; Wallace 2003:103-107.

¹⁰⁶⁹ Krackhardt 2005:342; Eriksson 2003:186.

¹⁰⁷⁰ Sections 101-107 of SOX. Wallace 2003:104.

¹⁰⁷¹ Martella et al 2004:61-63.

¹⁰⁷² Martella et al 2004:63.

¹⁰⁷³ Martella et al 2004:63.

¹⁰⁷⁴ Harris and Burns 2002:30.

¹⁰⁷⁵ Bartholmeusz 2002:581.

¹⁰⁷⁶ Bartholmeusz 2002:581.

corporation.¹⁰⁷⁷ In turn, corporate transparency contributes to the facilitation of reasonably well-functioning securities markets.¹⁰⁷⁸

Real-time disclosure¹⁰⁷⁹ is required on information concerning material changes in a company's financial conditions or operations. Quarterly reporting is required. Any trade that could significantly influence a company's stock price must be disclosed within two days of the transaction and posted on its website within three days. One of the causes of Enron's collapse was that off-balance sheet accounts were not disclosed.¹⁰⁸⁰ To prevent a recurrence thereof, it is now required that all off-balance sheet transactions must be disclosed. The lack of transparent reporting and credibility of financial reports contributed in part to the collapse of Steinhoff, similar to the collapse of Enron, directly linked to off-balance sheet accounts that were not disclosed.

2.6 CERTIFICATION REQUIREMENT

The CEO and CFO of public companies have to ensure that adequate internal corporate controls are implemented and checked 90 days before the certification of each report.¹⁰⁸¹ In accordance with SOX, reports are certified as not containing untrue statements and presenting a true and fair view of the company's financial situation.¹⁰⁸² Harsh penalties, including imprisonment, are imposed for filing untrue statements. Certification has the positive effect of emphasizing the importance of linking the audit report directly with the executives and not only the auditors.¹⁰⁸³

It should be noted that the United States Supreme Court in *US v Arthur Young and Co*¹⁰⁸⁴ already in 1984 placed an important role on the accountant who certifies the corporation's public financial reports. The Court declared that

¹⁰⁷⁷ Cunningham 1999:1137.

¹⁰⁷⁸ Cunningham 1999:1137.

¹⁰⁷⁹ Wallace 2003:104 explains real time disclosure as the rapid disclosure of current information.

¹⁰⁸⁰ Krackhardt 2005:347; Uberoi 2018:4; Wallace 2003:97; Wade 2002:97.

¹⁰⁸¹ Wallace 2003:104.

¹⁰⁸² Wallace 2003:105.

¹⁰⁸³ Krackhardt 2005:349.

¹⁰⁸⁴ *U.S. v Arthur Young & Co* 465 US 805 (1984).

"[b]y certifying a corporation's public financial reports, an independent certified public accountant assumes a public responsibility and "performs a different role": the accountant that makes this certification owes ultimate allegiance, not to a client, but to the corporation's creditors and stockholders, as well as to the investing public. This responsibility to function as a "public watchdog" mandates that the accountant maintain "total independence from the client at all times and requires complete fidelity to the public trust." ¹⁰⁸⁵

2.7 EXTERNAL AUDIT

Auditors should be independent of their clients, and this auditing independence is very important to investors as they must be able to rely on the financial statements. However, in the 1990s, accounting firms started also to offer their clients consulting services which were more profitable.¹⁰⁸⁶ Hajduka argues, and I agree with her, that the auditing function and consulting services are incompatible, especially because consulting services to their clients may directly influence the independence of the auditors.¹⁰⁸⁷ The major (Big Five) auditing firms have expanded their non-audit business after the auditor independence rule was amended in 1983. This has led to reduced investor confidence in the US equity markets.¹⁰⁸⁸ Hajduka also states that auditors should advise their clients on how to account for their money, and because of the ever-increasing pressure on corporations to report increases in profits, auditing independence is of vital importance.¹⁰⁸⁹ The collapse of Enron can, in part, be blamed on Arthur Andersen, especially because of the huge focus on consulting services to Enron of about \$50 million in 2000. This clearly influenced Arthur Andersen's independence.¹⁰⁹⁰ Courthold quotes that *"revelations of widespread accounting fraud and other misconduct by senior executives spiralled the firm into what was then the largest bankruptcy in history."* ¹⁰⁹¹ The role of the external auditors in Steinhoff's collapse is also partly due to the lack of independence and, just like with the collapse of Enron, directly linked to accounting fraud.

¹⁰⁸⁵ *U.S. v Arthur Young & Co* 465 US 805 (1984):817-818 cited in Lucci 2003:189.

¹⁰⁸⁶ Hajduka 2002:36.

¹⁰⁸⁷ Hajduka 2002:36.

¹⁰⁸⁸ Hajduka 2002:36.

¹⁰⁸⁹ Hajduka 2002:36.

¹⁰⁹⁰ Hajduka 2002:37.

¹⁰⁹¹ Skeel 2005: 131 quoted in Courthold 2010:55.

2.8 SHAREHOLDER AND STAKEHOLDER INTERESTS

Traditionally the interests of shareholders are taken into account and protected.¹⁰⁹² Shareholders are the owners of corporations and have the power to elect and remove directors.¹⁰⁹³ Furthermore, they only have indirect control over the appointment of managers, managers are elected and appointed by the board, and directors are elected by shareholders.¹⁰⁹⁴ Shareholders can only initiate changes in corporate by-laws and not the corporate charter.¹⁰⁹⁵ The shareholder approach is endorsed by the Delaware laws in the United States.¹⁰⁹⁶ In theory, if the board is faced with making strategic decisions, the objective of the shareholder informs the strategic decision.¹⁰⁹⁷ In the United States, there is a movement towards companies adopting institutional features of government.¹⁰⁹⁸ Fairfax contends that increased shareholder participation will enhance managerial accountability and prevent abuses of authority.¹⁰⁹⁹ Efforts to enhance shareholder participation, such as in Germany, Japan and Canada, is on the increase and have a valuable function and positive effect on corporate governance and share value.¹¹⁰⁰

Fairfax¹¹⁰¹ alluded to the controversy over the proper place of shareholder participation on whether institutional shareholders will utilize and maintain their shareholder power to improve corporate governance or will it translate to influence and undermine the efficiency of boards and advance their own personal agendas at the expense of the corporation.¹¹⁰² I am of the opinion that even in instances where shareholders cannot directly impact on decisions affecting corporate governance, shareholders exert indirect pressure on corporate directors by involving the public and rallying up the media, as was apparent in the Steinhoff collapse.

2.9 CONCLUSION

¹⁰⁹² Lund 2019:743; Kerr 2006:1066-1067. Bebchuk 2006:1812.

¹⁰⁹³ Owen 2003:173.

¹⁰⁹⁴ Owen 2003:174.

¹⁰⁹⁵ Ogbodo et al 2018 143; Fairfax 2008:3. Bebchuk 2006:10811.

¹⁰⁹⁶ Kerr 2006:1066; Eriksson 2003:188.

¹⁰⁹⁷ Licht 2011:17; Bebchuk 2006:10811-1812.

¹⁰⁹⁸ Coglianesi 2007:166.

¹⁰⁹⁹ Fairfax 2008:3.

¹¹⁰⁰ Fairfax 2008:4; Kerr 2006:1056; Cooney 2003:717.

¹¹⁰¹ Fairfax 2008:22.

¹¹⁰² Kerr 2006:1056-1066.

Post-Enron, numerous new federal corporate legislation have been passed, and amendments made to prevent corporate scandals, which included investment scams, corporate malfeasance, unethical conduct and conflicts of interests that contributed to the collapse of WorldCom,¹¹⁰³ Global Crossing,¹¹⁰⁴ Xerox,¹¹⁰⁵ Tyco,¹¹⁰⁶ Enron¹¹⁰⁷ and led to concerned investors withdrawing from the public securities markets and the tumbling of U.S stock markets.¹¹⁰⁸ As a result of the Enron and WorldCom scandals, SOX focuses mainly on audits, accounting and federalized corporate governance standards. Therefore, it does not focus on directors and is inadequate to resolve the problems of directors acting outside their fiduciary duties and duties of care raised in this thesis. In 2002, in addition to SOX, the New York Stock Exchange (the "Exchange") reviewed its corporate listing standards that were applicable to all companies that had listed common stock. The Exchange appointed a corporate accountant ability and listing standards committee ("the Committee") tasked with drafting proposals for corporate governance reforms to be codified in section 303 of the New York Stock Exchange's Listed Company Manual.¹¹⁰⁹

The Committee defined independent directors as those directors who have no material relationship with the listed company either as a shareholder, partner or officer of an organization related to the company. Proposals made by the Committee regarding effective boards included that listed companies have a majority of independent directors that exercise independent judgment in the fulfilling of their duties.¹¹¹⁰ To increase the authority and independent role of directors, it was proposed that listed companies must have a separate compensation committee, audit committee and nomination committee,

¹¹⁰³ Wallace 2003:103. WorldCom collapse involved accounting irregularities wherein earnings were inflated. Anderson 2008:1082 stated WorldCom was the largest bankruptcy filing in the history of the USA. Grossman 2005:578; Hopt 2003:222-223; Ronen 2002:39-40; Eriksson 2003:191; West 2009-13; Owen 2003:170 noted that WorldCom similar to Enron overstated its earnings and in addition to the restatement of earnings twenty percent of the workforce were eliminated.

¹¹⁰⁴ Wallace 2003:102. Global Crossing Ltd together with its auditor Arthur Andersen were investigated by the U.S Securities and Exchange commission for fraudulently inflated income and applied for bankruptcy. Ronene 2002:40.

¹¹⁰⁵ Eriksson 2003:191; Ronen 2002:38-39.

¹¹⁰⁶ Wallace 2003:102. Tyco International was investigated for self-dealing by insiders and tax evasion. Eriksson 2003:191.

¹¹⁰⁷ Murphy 2008:140; Wade 2002:97-104; Anderson 2008:1087; Grossman 2005:578; West 2009-13.

¹¹⁰⁸ Anderson 2008:1082; Rochvarg 2003:89.

¹¹⁰⁹ Owen 2003:181.

¹¹¹⁰ NYSE Report 2002:1-2; Owen 2003:181-182.

each consisting solely of independent directors.¹¹¹¹ To encourage the autonomy of independent directors, a proposed rule required that independent directors have regular open discussion sessions in the absence of management.¹¹¹²

There are marked differences between the corporate governance frameworks of the USA and the corporate governance framework applicable to South Africa.¹¹¹³ In the USA, corporate governance is subjected to mandatory regulation under SOX, numerous voluntary codes of corporate governance that act as guidelines to boards and shareholders, as well as rules of the stock exchanges.¹¹¹⁴ Whereas in South Africa, corporate governance broadly follows Anglo-American examples with the exception of the stakeholder approach of the King I and King II reports and is based on voluntarism.¹¹¹⁵ In the USA, stakeholders' interests are not acknowledged, and the contractarian model severely limits the stakeholder power of employees.¹¹¹⁶ No direct power or authority is given to employees or trade unions to participate directly in the governance of the corporation in contrast with South Africa, the interests of stakeholders and employees are acknowledged and protected.¹¹¹⁷

While the South African Companies Act 2008 allows for greater organisational flexibility,¹¹¹⁸ the Act i) establishes the minimum standards for shareholder and other stakeholder participation in corporate affairs; ii) determines the qualifications of corporate directors; iii) mandates audits of corporate financial statements; and iv) mandates directorial oversight of such audits by a board audit committee, in a manner similar to that required by SOX.¹¹¹⁹

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¹¹¹¹ NYSE Report 2002:2-15; Owen 2003:180-181.

¹¹¹² NYSE Report 2002:2; Owen 2003:181.

¹¹¹³ Wiese 2018:206.

¹¹¹⁴ Hill 2019:511; Anand 2006:229.

¹¹¹⁵ West 2009:10-11.Olson 2010:225-226.

¹¹¹⁶ Clarke 2005:366; Shi 2007-200-203; Anderson 2008:1081

¹¹¹⁷ Wiese 2018:21; Shi 2007-197.

¹¹¹⁸ Olson 2010:220.

¹¹¹⁹ Olson 2010:220; Shu-Acquaye 2007:586 noted that SOX imposes mandatory provisions "one-size-fits-all approach" for all US companies "Mandatory provisions" are typically non-negotiable laws or regulations that require individuals or corporations to comply with certain rules or standards affected by them.

3.1 INTRODUCTION

In Germany, the corporate governance system is based on employee involvement and is founded on a two-tier board system¹¹²⁰ and regulated by the German Corporate Governance Code ("GCCC"),¹¹²¹ the German Stock Corporations Act 1965¹¹²² and the Codetermination Acts.¹¹²³ The two-tier board system separates the corporation into those who manage the corporation from those who oversee the operations of the corporation.¹¹²⁴ The executive board manages the corporation and is responsible to represent the corporation, while the supervisory board controls the executive board.¹¹²⁵ As described by Shi, one board member cannot sit as a member of another board because German law requires a dual board system (Aktiengesellschaft) that consists of a management board (Vorstand) and a supervisory board (Aufsichtsrat).¹¹²⁶ As noted by Owen, the Aktiengesellschaft is comparable to the American version of a publicly traded corporation.¹¹²⁷ Extensive provisions in the German Code and the German Stock Corporation Act regulate the management board and supervisory board.¹¹²⁸

Escher-Weingart explains that stakeholder capitalism continues to prevail in Germany over shareholder capitalism and includes an inflexible labour regime.¹¹²⁹ German law restricts the ownership of funds to ten per cent of the voting shares of the corporation.¹¹³⁰

As explained by Olson, the major difference between the corporate governance practices in the United States and Germany are the unitary board system in the United States and the two-tier board system in Germany.¹¹³¹ In a unitary board, a member of the board of directors may also be an officer, in a two-tier board, a member of the management board

¹¹²⁰ Wiese 2018:191; Majmudar 2021:87; Shi 2007:201; Harnos 2015:93; Du Plessis 1996:20; Clarke 2006:1.

¹¹²¹ <http://www.corporate-governance-code.de/eng/kodex/index.html> Accessed 04/04/2023.

¹¹²² The Aktiengesetz (AktG); Moss 2020:65; Harnos 2015:97.

¹¹²³ The Codetermination Acts of 1951, 1976 and 2004. As noted by Oquendo 2001:980 German law assigns half of the supervisory council seats to employees if a public corporation employs over two thousand employees.

¹¹²⁴ Owen 2003:168; Olson 2010:219-232.

¹¹²⁵ Harnos 2015:93; Du Plessis 1996:21.

¹¹²⁶ Shi 2007-200-201.; Du Plessis 1996:21.

¹¹²⁷ Owen 2003:174.

¹¹²⁸ Hopt 2017:122.

¹¹²⁹ Escher-Weingart 1999:243.

¹¹³⁰ Escher-Weingart 1999:247.

¹¹³¹ Olson 2010:227-230; Owen 2003:174-175.

is prohibited from also sitting on the supervisory board of the same corporation.¹¹³² In Germany, codetermination laws are endorsed to ensure the representation of employees on the supervisory boards of corporations.¹¹³³ As explained by Moss, it is the duty of the management board to prioritize the interests of the employees and the company as a whole over the interests of stakeholders and individual shareholders (the duty of care and business judgment rule are equally important).¹¹³⁴

3.2 BOARD COMPOSITION

The corporate law system of Germany is founded on a two-tier board system which consists of the managing board, also referred to as the executive board¹¹³⁵ and the supervisory board.¹¹³⁶ The German Code contains principles and recommendations for both the management board and the supervisory board.¹¹³⁷ It highlights the obligation to consider the interests of all shareholders and stakeholders related to the company and ensure its sustainability and continued existence.¹¹³⁸ Employees and stakeholders form part of the supervisory board that elects board members and are, therefore, also shareholders.¹¹³⁹ The majority of investors in Germany are large investment blocks and financial institutions.¹¹⁴⁰ An important component of stakeholders are employees, and it is the responsibility of management to reconcile and counsel the interests between employees, other stakeholders and shareholders.¹¹⁴¹

Cunningham explains that the management board (*Vorstand*) is responsible for managing the corporation. It represents the corporation in third-party dealings, and it is also required to submit regular reports to the supervisory board.¹¹⁴² On the other hand, the supervisory board (*Aufsichtsrat*) has the responsibility to appoint and removes the members of the

¹¹³² Owen 2003:175.

¹¹³³ Owen 2003:175-176.

¹¹³⁴ Moss 2020:75.

¹¹³⁵ Consists of executives the main function is representing the company and managing its business affairs. Moss 2020:75; Harnos 2015:93-94; Cunningham 1999:1140; Olson 2010:227-228.

¹¹³⁶ The main function is monitoring the management board and attending to the day-to-day business operations. Harnos 2015:94; Olson 2010:228; Cunningham 1999:1140. See Du Plessis 1996:20-46; for a comprehensive discussion of the German board system.

¹¹³⁷ Shi 2007:200-203; Moss 2020:64-90.

¹¹³⁸ German Corporate Governance Code 2022:2.

¹¹³⁹ Fairfax 2008:31; Shi 2007:200; Moss 2020:64-90; Olson 2010:232.

¹¹⁴⁰ Owen 2003:179.

¹¹⁴¹ Majmudar 2021:87; Shi 2007:201; Moss 2020:74; Clarke 2006:1.

¹¹⁴² Cunningham 1999:1140; Jungmann 2006:432; Du Plessis 1996:21.

management board, and it must oversee the management of the corporation.¹¹⁴³ The management board is responsible for managing the internal affairs of the company on a day-to-day basis and also sets up long-term goals and guidelines.¹¹⁴⁴ The management board and chairman are selected by the supervisory board, and the appointment may be extended or renewed on condition that the renewal or extension does not exceed five years.¹¹⁴⁵

The supervisory board comprises an equal amount of non-executive directors representing employees and shareholders.¹¹⁴⁶ Strine explains that under the German codetermination system, the employee-elected representatives must hold at least half of the seats (and shareholder-elected representatives the other half) on the second-tier supervisory board of large companies, and the employees must have enforceable voting rights.¹¹⁴⁷ Even though the supervisory board cannot make management decisions, it can determine that “certain actions or business measures contemplated by the management board require its prior approval.”¹¹⁴⁸ The supervisory board must also approve the annual accounts as well as intervene in cases where the interests of the company are seriously affected.¹¹⁴⁹ In other words, German corporations must cooperate with employee councils as management needs to consult the employees on numerous matters regarding corporate policy.¹¹⁵⁰ As noted by Baron, codetermination is efficient and beneficial as the monitoring of management is thereby increased, and the overall productivity is increased.¹¹⁵¹ In the instance of Steinhoff, there were no labour representatives on the board, writer suggests that if labour representatives were on the board, the interest of management, shareholders and labour would have been represented, and active monitoring of the management board and committees would have resulted.¹¹⁵² At an operational level, the benefits of labour representatives will ensure transparency and the free flow of information, creating an

¹¹⁴³ Cunningham 1999:1140; Jungmann 2006:432; Du Plessis 1996:21.

¹¹⁴⁴ Jungmann 2006:433.

¹¹⁴⁵ Owen 2003:178-179; Jungmann 2006:432; Du Plessis 1996:24.

¹¹⁴⁶ Ogbodo et al 2018:142. Majmudar 2021:86; Shi 2007-203; Moss 2020:75; Baron 2020:458.

¹¹⁴⁷ Strine 2016:1252; Cunningham 1999:1141. Trimble 2019:174 noted that the German co-determination system is based on the notion that employees are investors in the corporation and should be brought into the governance of the corporation.

¹¹⁴⁸ Cunningham 1999:1141.

¹¹⁴⁹ Jungmann 2006:432.

¹¹⁵⁰ Cunningham 1999:1140.

¹¹⁵¹ Baron 2020:459.

¹¹⁵² Trimble 2019:174-175.

environment with fewer disruptions, costly strikes and higher productivity.¹¹⁵³ The presence of labour representatives improves the adversarial relationship between management and labour, wherein labour representatives are given the opportunity to raise their concerns and improves productivity.

Strine indicates that in Austria, Denmark, Luxembourg, Sweden, the Czech Republic, Slovenia, Slovakia, and Hungary, employees or employee representatives will have one-third of the seats on company boards.¹¹⁵⁴ Employee participation is also required in France and Ireland pertaining to certain aspects of corporate governance.¹¹⁵⁵

The German code allows a person membership of up to ten supervisory boards but recommends that a person be limited to five supervisory boards.¹¹⁵⁶ The German code requires that members of the supervisory board must be sufficiently independent¹¹⁵⁷ and report on conflicts of interest.¹¹⁵⁸ Supervisory board members are prohibited from pursuing personal interests in relation to the company¹¹⁵⁹ or acting as either advisors or directors for competitors.¹¹⁶⁰ The principal duty of the supervisory board is to monitor and oversee the management board. Other functions of the supervisory board include the review of major business decisions, the nomination, appointment and termination of employment of members of the management board, and determining executive directors' compensation.¹¹⁶¹

3.2.1 DUTIES OF DIRECTORS

In contrast with the individual derivative action in the USA, Germany has a group approach to the derivative action.¹¹⁶² The two-tiered board system in Germany consists of a management board and a supervisory board. The sole purpose of the supervisory board is to effectively control the management board and fulfil its oversight function. The role of

¹¹⁵³ Baron 2020:460-461.

¹¹⁵⁴ Strine 2016:1252.

¹¹⁵⁵ Strine 2016:1252.

¹¹⁵⁶ S 5.4.3. Trimble 2019:174-175.

¹¹⁵⁷ S 5.4.1.

¹¹⁵⁸ S 5.5.2.

¹¹⁵⁹ S 5.5.1.

¹¹⁶⁰ S 5.4.2. Trimble 2019:174-175.

¹¹⁶¹ Hopt 2017 137; Clarke 2005:364-365; Owen 2003 175-176.

¹¹⁶² Cooney 2003:726-727 noted that it is difficult for shareholders and individuals to muster the shares and financial resources necessary to institute derivative action. Trimble 2019:173-174.

the supervisory board in the Steinhoff collapse is also due in part to the lack of oversight of the supervisory board and directly linked to the supervisory board's failure to successfully fulfilling its "watchdog" function. Under German law, the supervisory board and not the shareholders have the power to decide whether to institute the action and have the responsibility to enforce managerial duties and pursue claims.¹¹⁶³

As stated by Cooney, the biggest obstacle to shareholder suits in Germany is the doctrinal framework stipulating that directors only owe duties to the corporation, and any violation of these duties is only indirect and regarded as legally irrelevant.¹¹⁶⁴ However, if the supervisory board fails to act, the shareholders may request a shareholder meeting. This group of shareholders may not institute derivative action directly and must act through a special representative.¹¹⁶⁵

3.3 AUDIT COMMITTEE

The German code¹¹⁶⁶ determines that the chairperson of the audit committee should neither be a former management board member nor a supervisory board chairperson. No mention is made regarding the rotation of auditors. The supervisory board examines the annual financial statements and auditor's report, and its findings are reported to the general meeting of shareholders.

3.4 EMPLOYEES REPORTING AND DISCLOSURE

Frequent reporting and continuous disclosure keep shareholders and stakeholders updated.¹¹⁶⁷ Companies must issue an annual report within 90 days of the end of the financial year and interim reports within 45 days after the end of the reporting period. The management board prepares the annual report under the supervision of both the

¹¹⁶³ Cooney 2003:725-726.

¹¹⁶⁴ Cooney 2003:726.

¹¹⁶⁵ Cooney 2003:725-727 noted that this group of shareholders must represent five percent of the stated capital for a minimum of three months. Cooney 2003:717 noted in contrast with Japan that does not require a shareholder to represent other shareholders.

¹¹⁶⁶ S 5.3.2.

¹¹⁶⁷ Hopt 2017 137; Clarke 2005:365.

supervisory board and the auditor. All reports are prepared using generally accepted accounting principles (GAAP) and are accessible to the public.

As per the German code, if a company's stock price can be significantly affected by any non-public facts, it must be disclosed.¹¹⁶⁸ Under the Act, broadened power is given to South African trade unions to access company financial statements for business rescue. Additional information must be provided if the board provides financial assistance to any director.¹¹⁶⁹

3.5 CERTIFICATION REQUIREMENT

The CEO and CFO have to certify the annual reports represent a true and fair view.¹¹⁷⁰

3.6 SHAREHOLDER AND STAKEHOLDER INTERESTS

Fairfax noted that, similarly to Japan and the United Kingdom, shareholders have been more involved in challenging corporate governance practices and have been active in opposing company resolutions and challenging CEOs that are underperforming.¹¹⁷¹ Large banks are the majority of shareholders.¹¹⁷² Two group holders exist in Germany, creditors and employees. In Germany, the stakeholder module is more complex, and it promotes the interests of employees.¹¹⁷³ Employees could play an important role in monitoring management by participating in corporate governance and as shareholders.¹¹⁷⁴ The German system of mandatory involvement of employees illustrates a system of codetermination of not only the interests of shareholders but also the interests of other stakeholders, including employees are taken into account.¹¹⁷⁵ Employees' voices are realized on various platforms, the most powerful form is that of board-level representation, and Germany's codetermination policy offers a unique approach to board-level

¹¹⁶⁸ S 3.5.2.

¹¹⁶⁹ Sec 45 (5).

¹¹⁷⁰ Krackhardt 2005:349.

¹¹⁷¹ Fairfax 2008:20-22 refers in particular to the ousting of the head of Deutsche Börse in 2005.

¹¹⁷² Moloi 2008:29; Shi 2007:205; Owen 2003:179.

¹¹⁷³ Clarke 2005:366; Shi 2007:203.

¹¹⁷⁴ Krackhardt 2005:353; Shi 2007:200-201; Moss 2020:74; Harnos 2015:97; Owen 2003:179.

¹¹⁷⁵ Moloi 2008:29; Shi 2007:204; Moss 2020:70; Harnos 2015:98; Trimble 2019:174-175.

representation.¹¹⁷⁶ Employees are represented on the supervisory boards.¹¹⁷⁷ This practice of accommodating employee stakeholder groups on the supervisory board has been a practice for an extended period of time.¹¹⁷⁸ However, compared to South Africa, these employee stakeholders have little direct power. In South Africa, shareholders, directors, officers or trade unions representing employees may initiate proceedings to prevent the corporation from doing anything inconsistent with the Act.¹¹⁷⁹ Employees are provided with the opportunity to have a director declared delinquent¹¹⁸⁰ and institute derivative action to claim financial losses directly from the board.¹¹⁸¹ Section 61 (8) (d) of the Act allows shareholders to raise any item during the annual general meeting without providing advance notice to allow the board of directors or management to prepare an organized response to such matter, in contrast with the United States shareholders may not directly raise agenda items without prior notice to the meeting.¹¹⁸² The lack of active involvement of Steinhoff shareholders during its annual meetings is also a contributory factor to the collapse of Steinhoff.

The corporate governance scandals that occurred in Siemens¹¹⁸³ and Volkswagen¹¹⁸⁴ have raised concerns regarding the effectiveness of labour representation on the supervisory boards of these companies. Wilson mentioned that the governance structure of Volkswagen did not inspire confidence; the majority of the board of directors was not independent, several family members were seated on the board, including two nieces of the former chairperson, without proper disclosure of their credentials, and the audit

¹¹⁷⁶ Sefara 2019:20; Shi 2007:201; Moss 2020:64-90.

¹¹⁷⁷ Supervisory boards appoint the management board, advises the management board, and follows up the management board's compliance with the company statutes, the law and business objectives. Shi 2007:208; Moss 2020:77; Owen 2003:179.

¹¹⁷⁸ Shi 2007:208-209 stated that there has been a long history of labour co-determination in Germany of employee-representatives on the board of directors. Moss 2020:65 stated that in Germany block holders and banks have a strong influence on the corporate legal system.

¹¹⁷⁹ Olson 2010:225-226.

¹¹⁸⁰ Section 162 (2) of the Act. Olson 2010:226.

¹¹⁸¹ Section 165 (2) of the Act.

¹¹⁸² Olson 2010:243.

¹¹⁸³ Donaldson 2007 states that the Siemens scandal involved the payment of bribes <https://www.knowledge.wharton.upenn.edu/article/hit-by-an-earthquake-how-scandals-have-led-to-a-crisis-in-german-corporate-governance/> Accessed 24/08/2022.

¹¹⁸⁴ Donaldson 2007 states that the Volkswagen scandal has been attributed to "Labor-management coziness." In order to receive the support from the employee representatives on the supervisory board, for Volkswagen's request for working longer hours and corporate restructuring the company's management offered money, bribes and vacations to union members to secure votes. <https://www.knowledge.wharton.upenn.edu/article/hit-by-an-earthquake-how-scandals-have-led-to-a-crisis-in-german-corporate-governance/> Accessed 24/08/2022.

committee was not independent, and the company lacked a compensation committee.¹¹⁸⁵ The labour representatives neglected the interests of the labour and finally drove their respective companies into crisis.¹¹⁸⁶ Consequently, studies are being conducted to propose modifications to the existing supervisory codetermination.¹¹⁸⁷

3.7 CONCLUSION

In Germany, compliance with the German Code is regulated by the corporation law rather than the stock exchange rules. South Africa's corporate governance comprises the Act, the King IV Report on common governance law and the JSE exchange listing requirements. There are no mechanisms of legal enforcement for non-compliance.¹¹⁸⁸ In accordance with the German code, listed companies are required to disclose in their annual report to what extent they complied with the recommendations or explain their deviation therefrom.¹¹⁸⁹ Any non-compliance with suggestions does not have to be published. In South Africa, the application of King IV is "apply and explain". Any non-compliance must reflect in the company's annual report. In South Africa, there are no employee representatives on the board. Similarities between the governance frameworks are the emphasis on accountability and transparency, the application of the business judgment rule, the chairperson of the board and the chairperson of the audit committee must not be the same person, and the compensation of the board members must be disclosed. All shareholders shall be treated equally, and the same information will be distributed to all shareholders.¹¹⁹⁰

4 AUSTRALIA

4.1 INTRODUCTION

¹¹⁸⁵ Wilson J 2015:5.

¹¹⁸⁶ Wilson J 2015:1 touched on the allegations that Volkswagen installed defective devices on its cars to evade the emissions requirements.

¹¹⁸⁷ Donaldson 2007 states that a commission has been appointed by Chancellor Angela Merkel to re-evaluate the system of codetermination and recommend whether it should be modified. The Federal Association of German Employers Confederations supports a possible option of limiting employee representation on supervisory boards to one-third. <https://www.knowledge.wharton.upenn.edu/article/hit-by-an-earthquake-how-scandals-have-led-to-a-crisis-in-german-corporate-governance/> Accessed 24/08/2022.

¹¹⁸⁸ The rules consist of recommendations and suggestions.

¹¹⁸⁹ Krackhardt 2005:332.

¹¹⁹⁰ Wiese 2018:195. Moloi 2008:30.

In contrast with the USA's mandatory corporate governance regime, the Australian corporate governance regime is an enabling or voluntary regime; and it denotes a corporation's choice to adopt corporate governance practices of standards in the absence of a mandatory legal requirement to do so.¹¹⁹¹ Judge Romer noted in *Re City Equitable Fire Insurance Corporation*¹¹⁹² that the Australian company law is mainly based on English law. The Australian corporate governance regime revolves around the Australian Stock Exchange ("The ASX") guidance.¹¹⁹³ The corporate governance framework in Australia, similar to the Anglo-US counterparts, focuses squarely on shareholders' rights and consists of the Corporations Act of 2001, the Australian Securities Exchange Ltd (ASX) and the Australian Securities and Investment Commission (ASIC).¹¹⁹⁴

In 2003 the Principles of Good Corporate Governance and Best Practice Recommendations (Australian Principles) were approved by the Corporate Governance Council (The Council).¹¹⁹⁵ The Australian Principles apply to companies listed on the ASX and provide guidance and recommendations on achieving best practices in governance¹¹⁹⁶ The Australian principles are not mandatory. It comprises of self-regulation and codes of practice.¹¹⁹⁷ The Council considered that companies legitimately adopt different governance practices based on various factors, including their history, size, corporate culture and complexity. Therefore, the Council do not seek to prescribe corporate governance practices to listed companies.¹¹⁹⁸

Listing Rule 4.10.3 requires listed companies to include in their annual report a corporate governance statement¹¹⁹⁹ containing disclosure of noncompliance and a completed Appendix 4G-form (Key to Disclosures Corporate Governance Council Principles and

¹¹⁹¹ Anand 2006:233-234.

¹¹⁹² *Re City Equitable Fire Insurance Corporation Ltd* 1925 Ch 407 as cited by Lee 2005:58.

¹¹⁹³ Anand 2006:232.

¹¹⁹⁴ Wiese 2018:183; Clarke 2006:1.

¹¹⁹⁵ <https://www2.asx.com.au/about/corporate-governance> Accessed 04/08/2022.

¹¹⁹⁶ Principle 1.1; Anand 2006:232.

¹¹⁹⁷ Shi 2007:198.

¹¹⁹⁸ Australian Corporate governance principles and recommendations 2019:1.

¹¹⁹⁹ A statement as defined in Listing Rule 19.12 which discloses the extent to which a company has followed the recommendations set by the ASX Corporate Governance Council during a particular reporting period.

Recommendation).¹²⁰⁰ Each listed company must disclose in its annual corporate governance statement the extent to which it followed the recommendations. Suppose the company has not followed a particular recommendation. In that case, it must be identified separately in its corporate governance statement the reasons for not following the recommendation instead of (if any) alternative governance practices it adopted in lieu of the recommendation during that period. Appendix 4 G¹²⁰¹ is not a substitute for the corporate governance statement. Both documents must be submitted simultaneously.¹²⁰² Voluntary compliance with these codes and guidelines is significant for promoting transparency, ethical leadership, responsible business practices and accountability. Corporations that implement good governance codes and practices are often viewed more favourably by employees, clients, shareholders and stakeholders, which can ultimately benefit the organizations' reputation and financial performance.

4.2 BOARD COMPOSITION

4.2.1 DUTIES OF DIRECTORS

In 1869 the English case of *Turquand v Marshall*,¹²⁰³ attention was given to the directors' duty of care, skill and diligence. The Appeal Court decision in *Daniels v Anderson*¹²⁰⁴ represents the pinnacle of the development of directors' duty of care, skill and diligence, and it is worth citing the parts where the court discussed whether a director owed a duty of care, the tort of negligence as the basis of directors' duty of care, skill and diligence and whether that duty was breached:

The court recognized

¹²⁰⁰ The Appendix 4G serves a dual purpose. It assists readers to locate the governance disclosures made by a listed entity under Listing Rule 4.10.3 and under the ASX Corporate Governance Council's recommendations. It serves as a verification tool for listed companies to confirm that they have met the disclosure requirements of Listing Rule 4.10.3; Anand 2006:232.

¹²⁰¹ Annexure A

¹²⁰² Listing Rule 4.7.3.

¹²⁰³ *Turquand v Marshall* (1869) LR 4 Ch App 376 discussed in Du Plessis 2010:271

¹²⁰⁴ *Daniels v Anderson* 1995 37 NSWLR 439 as cited by Lee 2005:61-62. Grossman 2005:576 ascertains that directors must in addition to their statutory duties also adhere to their common law duties to act bona fide in the best interests of the company

"[that] Directors must be allowed to make business judgments and business decisions in a spirit of enterprise untrammelled by the concerns of conservative investment trustees.... Great risks may be taken in the hope of commensurate rewards. If such ventures fail, how is the undertaking of it to be judged against an allegation of negligence by the entrepreneur? In our opinion the concept of negligence which depends ultimately 'upon a general public sentiment of moral wrongdoing for which offenders must pay'¹²⁰⁵ can adapt to measure appropriately in the given case whether the acts or omissions of an entrepreneur are negligent. We are of the opinion that a director owes to the company a duty to take reasonable care in the performance of the office. As the law of negligence has developed no satisfactory policy ground survives for excluding directors from the general requirement that they exercise reasonable care in the performance of their office. A directors' fiduciary obligations do not preclude the common law duty of care. The duty is a common law duty to take reasonable care owed severally by persons who are fiduciary agents bound to exercise the powers conferred upon them for private purposes or for any purpose foreign to the power and placed."¹²⁰⁶

According to Du Plessis, the crux of *Daniels v Anderson*¹²⁰⁷ is that it deals with the liability of directors for negligence. The cause of action was based on a claim for common-law damages, in particular, the tort of negligence, and not based on a breach of any equitable or fiduciary duty.

Although previous corporate legislation did not contain provisions dealing with the general duties of directors, Australia and New Zealand broke away from this tradition. Currently, both the Australian Corporations Act of 2001¹²⁰⁸ and the New Zealand Companies Act 105 of 1993¹²⁰⁹ contain provisions dealing with directors' general duties.¹²¹⁰ Section 232 (4) of the Australian Companies Act was amended by Section 180 (1) of the Companies Act.¹²¹¹

¹²⁰⁵ *Donohue v Stevenson* [1932] AC 562 at 580 quoted in Du Plessis 2010:272-273.

¹²⁰⁶ *Daniels v Anderson* 1995 37 NSWLR 668 as cited by Du Plessis 2010:272-273.

¹²⁰⁷ *Daniels v Anderson* 1995 37 NSWLR 652-68. Quoted in Du Plessis 2010:272.

¹²⁰⁸ Australian Corporations Act ss 180-184; Esser and Du Plessis 2007:346.

¹²⁰⁹ New Zealand Companies Act ss 131,133,137 and 138; Esser and Du Plessis 2007:346.

¹²¹⁰ Esser and Du Plessis 2007:346.

¹²¹¹ Lee 2005:61-62 noted "the amended Section 180 of the Companies Act Section 180(4) of the Companies Act dealing with, Care and diligence - directors and other officers, provides:

(1) A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:

The effect of the amendment is that a balance is being created between objective and subjective considerations when ascertaining the liability of company directors (both executive and non-executive directors) for breach of the duty of care and diligence.

As alluded to by Du Plessis in South African law, the distinction between common-law remedies and equitable remedies is insignificant in contrast with Australian law, where this distinction is important.¹²¹² In South African law, common law duties (including the duty of care and skill as well as directors' fiduciary duties) are divided into common law duties (duty of care and diligence) and duties in equity (fiduciary duties).¹²¹³ In South Africa, the form of fault that will be required if a court has to consider whether a director has breached his common law duty of care, skill and diligence is negligence as judged against the standard of a reasonable person. Therefore, objective standards of care and diligence are required from South African directors.¹²¹⁴

4.3 THE BUSINESS JUDGMENT RULE

Lee described a business judgment as any decision to take or not to take in respect of a matter relevant to the business operations of a company. Lee referred to the case of *Re City Equitable Fire Insurance Corporation*,¹²¹⁵ where Romer J emphasized that directors are not held liable for the mere errors of judgment but are required to use a degree of care similar to which an ordinary man might be expected to take in similar circumstances.¹²¹⁶

-
- a. *Were a director or officer of a corporation in the corporation's circumstances; and*
 - b. *Occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.*

(2) *A director or other officer of a corporation who makes a business judgment is taken to meet the requirements of subsection (1) and their equivalent duties at common law and in equity, in respect of the judgment if they*

- a. *Make the judgment in good faith and for a proper purpose; and*
- b. *Do not have a material personal interest in the subject matter of the judgment; and*
- c. *Inform themselves about the subject matter of the judgment to the extent they reasonably believe to be appropriate; and*
- d. *Rationally believe that the judgment is in the best interest of the corporation (the judgment is a rational one unless the belief is one that no reasonable person in their position would hold.)"*

¹²¹² Du Plessis 2010:271.

¹²¹³ Du Plessis 2010:271-272.

¹²¹⁴ Du Plessis 2010:263.

¹²¹⁵ *Re City Equitable Fire Insurance Corporation Ltd* 1925 Ch 407 as cited by Lee 2005:58.

¹²¹⁶ Lee 2005:58-59.

Initially, it seems that an essentially subjective test has been laid down by the court to objectively consider if a director performed his duties to a degree of skill that may reasonably be expected from a person of his knowledge or experience. The court's application of this predominantly subjective test that imposes a relatively low burden on company directors, as they are not required to possess any special skill, which often results in a lesser likelihood of liability ensuing, was viewed as out of step with modern corporate governance practice. As a result, in addition to the common law duty of care, the common law duties of company directors have been codified, and it now imposes a higher objective standard of care. It is now expected that an officer of a corporation, in exercising his or her duties, must exercise a degree of diligence and care that a reasonable person in the same position would have exercised in the corporation's circumstances.¹²¹⁷ The codification resulted in the subjective test that existed in the common law, which was now changed to an objective "reasonable person" test, which required a much higher objective test from directors.¹²¹⁸

As Lee concluded:

*" [that] The BJR will protect those directors who make business judgments in good faith, and for a proper purpose, have acted on an informed basis without material personal interests and who have a rational belief that the decision is in the best interests of the corporation but will not protect them in cases of negligence, ill-informed or fraudulent decisions. If one of these requirements is not met, the rule will not operate."*¹²¹⁹

4.4 PRINCIPLES OF GOOD CORPORATE GOVERNANCE AND BEST PRACTICE RECOMMENDATIONS

Contrasting to Germany, Australia does have a one-tier board structure and not a two-tier board system.¹²²⁰ The provisions of the Australian principles of good corporate governance

¹²¹⁷ Section 232 (4) Australian Companies Act as cited by Lee 2005:59-60.

¹²¹⁸ Lee 2005:61 stated that directors are now required as per legislation and common law that directors are required to place themselves in a position to monitor and manage the company. Grossman 2005:576-577; Du Plessis 2010:263.

¹²¹⁹ Lee 2005:62.

¹²²⁰ Shi 2007:204; Harnos 2015:93-102.

and best practice recommendations are similar to certain provisions contained in King IV. The Australian principles will be identified and compared with South Africa's current corporate governance structures as contained in the King IV Report.

The provisions of the Australian principles apply to all companies listed on the ASX, regardless of whether they are established in Australia or elsewhere.¹²²¹ It was first introduced in 2003. A second edition was published in 2007, a third in 2014, and the fourth edition came into effect in January 2020. As explained by Wiese, the principles address emerging issues and best practices, informed by new concerns such as culture, transparency, values and trust.¹²²² The principles are based on the following eight core principles.¹²²³

4.4.1 Defined roles and management oversight

The principles recommend that a company have and disclose a board charter that sets out the roles and responsibilities of the board and management.¹²²⁴ Those matters expressly reserved to the board and those delegated to management will also be stipulated.¹²²⁵ A listed company should undertake appropriate background checks before appointing a director or senior executive and provide security holders with the relevant information to decide whether to elect or re-elect a director.¹²²⁶ The principles recommend that the company secretary be accountable directly to the board, through the chair, regarding all matters relating to the effective functioning of the board.¹²²⁷ The failure of the company secretary to effectively fulfil their duties, which included transparent reporting, provision of credible reports and lack of commitment, contributed to the collapse of Steinhoff. Each listed company should have a gender policy and set measurable objectives for achieving overall gender diversity in the board, management and workforce.¹²²⁸ The board plays an important oversight role in the corporate governance framework, and periodic performance reviews of the board, its committees, senior executives and individual directors are

¹²²¹ Australian Corporate governance principles and recommendations 2019:2.

¹²²² Wiese 2018:184. As stated by Clarke 2005:360 in Japan the influence of culture

¹²²³ Recommendations on the application of each principle are included.

¹²²⁴ Principle 1 of Australian principles 2019:6.

¹²²⁵ Recommendation 1.1 of Australian principles 2019:6; Walthall 1982:76.

¹²²⁶ Recommendation 1.2 of Australian principles 2019:7.

¹²²⁷ Recommendation 1.4 of Australian principles 2019:8.

¹²²⁸ Recommendation 1.5 of Australian principles 2019:9.

recommended. It is further recommended that external service providers be appointed to evaluate the board, and a non-executive director (such as the deputy chair or the senior independent director) should be responsible for the performance evaluation of the chairperson.¹²²⁹ A company must disclose whether a performance review process was completed during the reporting period after each reporting period.¹²³⁰

4.4.2 Structure of the board

As per the Australian principles, the board must be structured to perform its duties effectively, and it should collectively have the knowledge, skills, and commitment to perform its duties effectively and add value to the industry in which it operates.¹²³¹ It is recommended that the board has an appropriate number of independent non-executive directors¹²³² who can challenge management and hold them accountable and also represent the best interests of the listed entity and its shareholders and stakeholders as a whole rather than those of individual shareholders or interest groups.¹²³³ As alluded to by Shi, in Germany, both the executive and independent directors sit on a separate board from the management board, which contrasts with Australia, where both executives and independent non-executive directors sit on the same board. The company should have a nomination committee comprising a minimum of three directors, most of whom should be independent.¹²³⁴

The principles recommend that a company should have and disclose a board "skills matrix", setting out the mix of skills that the board currently has or is looking to achieve in its membership.¹²³⁵ It further recommends that the chairperson should be an independent director and not the same person as the CEO.¹²³⁶ The majority of the board directors should be independent.¹²³⁷ An induction program of newly appointed directors is

¹²²⁹ Recommendation 1.6 of Australian principles 2019:11.

¹²³⁰ Recommendation 1.7 of Australian principles 2019:11.

¹²³¹ Principle 2 of Australian principles 2019:12.

¹²³² Shi 2007:204; Walthall:77.

¹²³³ Recommendation 2.1 of Australian principles 2019:12. Clarke 2005:365.

¹²³⁴ If a board decides not to have a separate nomination committee it must be stated in the annual report and explain the processes in place to ensure succession planning issues are addressed and to ensure that the board has the required knowledge, balance of skills, experience, diversity and independence to enable it to discharge its duties effectively.

¹²³⁵ Recommendation 2.2 of Australian principles 2019:13.

¹²³⁶ Recommendation 2.5 of Australian principles 2019:15.

¹²³⁷ Recommendation 2.4 of Australian principles 2019:15.

recommended, and the periodic assessment of existing directors' skills, knowledge and experience to deal with new and emerging business and governance issues.¹²³⁸ ASX Recommendations and the German Code emphasize the importance of having independent directors, an "independent director" is defined by the ASX Recommendations as a director who is not a substantial shareholder of the company.¹²³⁹ Shi states that the ASX definition of independence should be amended to that of the German definition of an independent director as a director who is not a substantial shareholder of the corporation.¹²⁴⁰ In Steinhoff, the CEO and the chairperson's roles were not separated, and the composition of the board did not consist of the majority of non-executive directors. These factors contributed to the collapse of Steinhoff.

4.4.3 Promote a culture and lawful decision making

A culture of acting lawfully, responsibly, and ethically should be instilled and maintained across the company.¹²⁴¹ Several policies¹²⁴² are recommended to create an ethically sound culture. These policies must be linked to the value statement of the company. Material incidents and breaches reported under the whistleblower and anti-bribery and corruption policy must be reported to the board or a committee of the board, as these may indicate issues with the company's culture.¹²⁴³

4.4.4 Integrity of reports

Appropriate processes must be implemented to ensure report integrity and verification.¹²⁴⁴ The board should elect the audit committee, which consists entirely of non-executive directors, of whom the majority must be independent directors. The chairperson must be an independent director, not the board's chairperson.¹²⁴⁵

4.4.5 Proper disclosure

¹²³⁸ Recommendation 2.5 of Australian principles 2019:15.

¹²³⁹ Shi 2007:204.

¹²⁴⁰ Shi 2007:205.

¹²⁴¹ Principle 3 of Australian principles 2019:16.

¹²⁴² Recommendation 3.1 of Australian principles 2019:17.

¹²⁴³ Recommendation 3.4 of Australian principles 2019:18.

¹²⁴⁴ Principle 4 of Australian principles 2019:19.

¹²⁴⁵ Recommendation 4.1 of Australian principles 2019:19.

A listed company must timeously disclose all matters that may have a material effect on the price or value of its securities.¹²⁴⁶ Proper disclosure ensures compliance and accountability at a senior executive level. It ensures that all investors have equal time and access to material information concerning the company, including financial, performance, ownership, and governance.¹²⁴⁷

4.4.6 Rights of security holders

Security holders must be provided with the necessary information to exercise their rights as security holders effectively. Fundamental to corporate governance is communication. Security holders must be provided with the necessary information to exercise their rights as security holders effectively. The communication policy should be disclosed, and shareholders and stakeholders should be able to access this information electronically. A listed company should establish an investor relations program facilitating effective two-way communication with investors.¹²⁴⁸ Investors expect information about listed companies to be readily available online. All relevant corporate governance information should be available on the company's corporate website with a "corporate governance" landing page from where all relevant corporate governance information can be accessed. There should be an intuitive and easily located link to this page in the navigation menu for the entity's website.¹²⁴⁹

4.4.7 Risk management

¹²⁴⁶ Principle 5 of Australian principles 2019:21. Interesting is the similar position in France. Fanto 1998:111 explains that French companies that make offers of their securities to the public or list securities on an exchange must disclose the information on their operations in a prospectus (*note d'information*). In addition, French companies must adhere to a system of continuous reporting based upon a company reference document (*document de référence*) used for listing and as an annual report. In the company reporting the financial accounts must include information on the company's past operations. The official company auditor (the *commissaire aux comptes*) must verify the company's financial results and internal controls and must report on any problems. There are also measures to ensure independence from management of the *commissaire*.

¹²⁴⁷ Wiese 2018:185.

¹²⁴⁸ Recommendation 6.2 of Australian principles 2019:24.

¹²⁴⁹ Recommendation 6.1 of Australian principles 2019:23.

A risk management framework should be established, and the effectiveness thereof should be periodically reviewed. The principles recommend that a risk management committee be established and consist of a minimum of three members. Most of them are independent directors and are chaired by an independent director.¹²⁵⁰ The effectiveness of the risk management committee should be reviewed annually by the board to ensure that the risk management framework identifies and manages contemporary and emerging risks such as conduct risk, digital disruption, cyber-security, privacy and data breaches, sustainability, and climate change.¹²⁵¹

4.4.8 Remuneration

Following Recommendation 8.1, a remuneration committee should be established.¹²⁵² The committee should consist of a majority of independent directors chaired by an independent director with a minimum of three members. The executive remuneration of directors and non-directors should be structured to attract, retain and motivate high-quality directors and non-directors and to align their interests with the creation of value for security holders and the entity's values and risk appetite.

5. CONCLUSION

The legal doctrine regarding corporate governance varies in the United States, Germany and Australia. Within government, legitimacy comprises of procedural legitimacy and substantive legitimacy.¹²⁵³ The Australian principles apply to only listed companies, whereas King IV applies to all entities. The Australian principles refer to key stakeholders,¹²⁵⁴ such as customers, employees, suppliers, creditors, lawmakers, and regulators. It does not refer specifically to other stakeholders, contrasting with the King IV Report. As stated by Clarke,¹²⁵⁵ the global effect of the US corporate governance has a

¹²⁵⁰ Recommendation 7.1 of Australian principles 2019:26.

¹²⁵¹ Recommendation 7.2 of Australian principles 2019:27.

¹²⁵² Australian Corporate governance principles and recommendations 2019:29.

¹²⁵³ Coglianese 2007:161.

¹²⁵⁴ Recommendation 3.1 of Australian principles 2019:16.

¹²⁵⁵ Clarke 2005:361. Globalisation refers to the neoliberal socioeconomic programs wherein the interests of shareholders are paramount. There is a complex interplay between different countries around the world that are accelerated with the interplay between national practice and regionalism. Shi 2007:210; Kerr 2006:1081; Bebchuk 2006:1784-1912.

clear global influence on the Australian and UK corporate governance practices wherein nations are becoming less hegemonic.

Cooney and other corporate legal academics strongly support the notion of a global convergence theory.¹²⁵⁶ The global convergence theory entails that corporate governance structures and the practices of large international corporations will globally resemble each other. The current debate is whether the convergence will be similar to the formal style of the USA style of corporate legal regimes or functional in the sense of a worldwide accord to the best practices.¹²⁵⁷ The downside of the convergence theory is the cost implication for organizations in changing corporate governance practices and structures as a result of cultural differences and the harmonization of international corporate governance standards and procedures.¹²⁵⁸

Cooney suggests that rather than considering convergence to the USA modality of shareholder derivative actions, accountability mechanisms should be developed, and current mechanisms be improved.¹²⁵⁹ Cooney suggests a team production model that separates traditional management from an independent non-stakeholder board of directors. The independent board of directors should compose independent non-stakeholder members to act as trustees and function as an independent mediating hierarchy that treats all stakeholders equally. Stakeholders make investments and cede power to the independent mediating hierarchy to protect.¹²⁶⁰

Corporate governance reforms must be aligned with established international "best practices" and how institutions will be able to facilitate and monitor compliance.¹²⁶¹

Di Lorenzo explored the issue of why have existing regulatory standards and enforcement policies led to repeated violations of law in the United States, and he draws a comparison between the philosophy motivating regulatory policy and action in the United States and

¹²⁵⁶ Cooney 2003:731.

¹²⁵⁷ Cooney 2003:731-734.

¹²⁵⁸ Cooney 2003:734-735.

¹²⁵⁹ Cooney 2003:735.

¹²⁶⁰ Cooney 2003:735-736.

¹²⁶¹ Alsharqawi and Alsharqawi 2019:69.

the United Kingdom.¹²⁶² In the United Kingdom, both the Prudential regulatory authority ("PRA") and Financial services authority ("FSA") has begun to recognize multiple cognitive influences on corporate behaviour beyond the influence of financial penalties.¹²⁶³ Di Lorenzo quoted the FSA acknowledged that rational decision-making did not fully and accurately predict and determine corporate outcomes and remarked:

*"[that] there are insights from behavioural economics, cognitive psychology and neuroscience which reveal that people often do not make decisions in the rational front of brain...assumed in neoclassical economics, but make decisions which are rooted in the instinctive part of the brain, and which at the collective level are bound to produce herd effects and thus irrational momentum swings."*¹²⁶⁴

In contrast, the deterrence strategy of the United States recognises behavioural influences on corporate behaviour and, therefore, consistently resorts to large financial penalties that have led to repeat violations.¹²⁶⁵ Transformation can only be achieved when it is supported by both the corporate business community and the public.¹²⁶⁶

I believe that the ideal would be to transform enforcement measures in such a manner that they interact with the many influences on corporate behaviour to incline the corporate decision-maker toward greater commitment to legal compliance. As alluded to by Jacobs, *"corporate governance is the hygiene of an organization, not the health"*.¹²⁶⁷

¹²⁶² Di Lorenzo 2017:207; Shi 2007:210.

¹²⁶³ Di Lorenzo 2017:250; Dbe 2003:282.

¹²⁶⁴ Di Lorenzo 2017:251.<https://perma.cc/39e6-4hgn> Accessed 10/06/2022.

¹²⁶⁵ Di Lorenzo 2017:251.

¹²⁶⁶ Dbe 2003:282; Lorenzo 2017:251; Quinn 2012:58.

¹²⁶⁷ Jacobs 2018:4.

CHAPTER 7: PREVENTION OF CORPORATE COLLAPSE

1. INTRODUCTION

This chapter will analyze the application of measures to prevent corporate collapse. It will examine the effects and likely challenges that could stand in the way of applying specific measures. Steinhoff is an example of how non-compliance and unethical behaviour leads to a company's collapse.

2. PREVENTATIVE MEASURES DEFINED

The quality of a company's corporate governance framework will determine whether it will be in a position to operate in an environment at risk of total disruption or collapse.¹²⁶⁸ A weak regulatory framework can undermine the effectiveness of corporate governance practices. Weak regulatory frameworks may result in unethical practices, corruption and, ultimately, corporate collapse, as was the position with Steinhoff. Preventative measures include the application of clawback clauses,¹²⁶⁹ fraud models, red flag ratios or carrying out due diligence screening to determine a company's financial health.

2.1. APPLICATION OF PREVENTATIVE MEASURES

A growing number of official enquiries,¹²⁷⁰ legislators, policymakers and law reformers are looking to international and comparative models in reviewing corporate governance guidelines.¹²⁷¹ As stated by Hazen, history has proven that legislative attempts to increase regulating the structures and compositions of boards, without taking into account the company's practical challenges, renders to be ineffective.¹²⁷² I agree with Di Lorenzo that emphasis on large penalties alone does not ensure greater corporate commitment to legal compliance, prevent recurring non-compliance, or deter future violations.¹²⁷³ Regulators

¹²⁶⁸ <https://www.cornerstonecapinc.com/wp-content/uploads/2015/09/VW-A-Case-Study-in-Failed-Governance-25-Sept-2015.pdf> Accessed 24/08/2022. Wilson 2015:1.

¹²⁶⁹ Majmudar 2021:93-97.

¹²⁷⁰ The Zondo commission on state capture report delivered 22 June 2022.

¹²⁷¹ Thomas 2012:454.

¹²⁷² Hazen and Hazen 2012:3.

¹²⁷³ Di Lorenzo 2017:211.

must consider the multi-cognitive influences on corporate behaviour during the decision-making process.¹²⁷⁴

Nel explained that during a decision-making process, the needed information would depend on whether it is a routine,¹²⁷⁵ non-routine or crisis situation.¹²⁷⁶ The decision-making process comprises of four elements, the gathering and evaluation of annual reports and organisational records, the processing of information, facilitating proactive participation of management in determining the company's strategic plan, and a constructive conflict management system. In the instance of Steinhoff, data integrity and the corporate behaviour of the board and failed oversight were major factors in the corporate collapse. In Steinhoff, the decision-making process lacked the participation of management as Jooste was described as a dominant CEO who did not take kindly to the opposition, and therefore the board was placed in a reactive position in stead of a proactive position.

Nel argues that corporate collapses, globalisation and complex business transactions have prompted current and potential investors' demand for more active engagement in corporate decision-making and updated and detailed information.¹²⁷⁷ To improve transparency and ensure accurate information, companies rely on their websites and annual reports to share accurate and additional information with investors.¹²⁷⁸ Sharpe notes that the effective monitoring of corporate governance practices is determined by active communication and consultation between CEOs and independent directors to ensure effective corporate governance processes are implemented.¹²⁷⁹ Nel and Sharpe addressed the issues of transparency, effective monitoring and accurate information but did not analyse corporate collapse prevention.

The G20/OECD Principles are intended to assist governments and companies in assessing and developing their corporate governance frameworks to be concise,

¹²⁷⁴ Di Lorenzo 2017:207.

¹²⁷⁵ During a routine situation, past information is normally utilised.

¹²⁷⁶ In a crisis situation, boards use strategic and independent information channels.

¹²⁷⁷ Nel 2019:17.

¹²⁷⁸ Nel 2019:16.

¹²⁷⁹ Sharpe 2012:41.

understandable and accessible to the international community.¹²⁸⁰ Increased focus on the structure and composition of boards impedes management's discretion, and boards are placed in a reactive position instead of being proactive in averting a corporate governance crisis.¹²⁸¹ I am of the opinion, however, that despite social, political, and legal outrage in reaction to corporate wrongdoing, (notwithstanding the clear provisions of the Public Finance Management Act,¹²⁸² the Act, and the King IV report), executives and directors are not committed to acting in the best interest of companies as implicated in corporate scandals and state capture.¹²⁸³ I agree with Di Lorenzo¹²⁸⁴ that the deterrent effect of enforcement policies must consider not only increased financial penalties as a mechanism to prevent future breaches of legal standards but also recognize multiple behavioural influences on corporate decision-makers, including corporate culture and behaviour influences.¹²⁸⁵ As noted by Di Lorenzo:

*"[that] the ideal would be to modify enforcement measures in such a manner that they interact with the many influences on corporate behavior so as to incline the corporate decision maker toward greater commitment to legal compliance."*¹²⁸⁶

2.2. RECOMMENDED MEASURES TO PREVENT CORPORATE GOVERNANCE COLLAPSE

2.2.1 INDEPENDENT MONITORING OF THE BOARD

Corporate governance practices and principles guide directors in making successful company decisions.¹²⁸⁷ Current corporate governance best practices are based on the assumption that independent directors¹²⁸⁸ will not be captured by management and will safeguard the company's assets to maximise shareholders' wealth. In the event of a conflict arising between stakeholders and shareholders' interests, it is the duty of the

¹²⁸⁰ G20/OECD Principles 2015:9.

¹²⁸¹ Sharpe 2012:5.

¹²⁸² Public Finance Management Act 1 of 1999.

¹²⁸³ <https://www.pwc.co.za/en/assets/pdf/king-iv-comparison.pdf> Accessed 21/07/2022; Wade 2002:97.

¹²⁸⁴ Di Lorenzo 2017:251.

¹²⁸⁵ Di Lorenzo 2017:250.

¹²⁸⁶ Di Lorenzo 2017:252.

¹²⁸⁷ Woolley and Costas 2005:2.

¹²⁸⁸ Those who do not have any financial or material interest through an employment, familial or investment relationship.

manager to endeavour a joint value creation.¹²⁸⁹ To strengthen their corporate governance role as gatekeepers and prevent large financial losses, the board of directors can follow the due diligence screening guidelines to identify red flags over the reporting period.¹²⁹⁰ A lack of trust between shareholders and directors is detrimental to both parties. The Codes of corporate governance recommend that companies appoint non-executive directors, audit committees consist of independent members, and the positions of chairperson and chief executive officer be separate.

The board of directors' duties comprise of oversight, monitoring and active participation in corporate governance, strategy development, risk management, and warranting the reliability of the financial reporting process. Boards are often challenged with differing oversight roles between monitoring and active participation in corporate governance. When corporations fail, the boards are almost, without doubt, blamed, as it replicates the high expectations placed upon the boards by regulators, shareholders and the public. Tung alluded that there are several probable explanations for these corporate failures.¹²⁹¹ First, the current definition of "independence" is too constricted as it does not consider the full range of a director's additional external incentives to favour management. Another probable cause is the information surroundings of companies differ. External directors will have more difficulty in obtaining transparent information than in transparent companies.¹²⁹² The effect of human character and the aspiration to "go with the flow" cannot be overlooked, especially the need of society not to disagree and to go alongside the majority and be a team player. These influences result in board members not being independent and as effective and objective as shareholders require them to be, in the instance of Steinhoff, the dominant influence of Jooste caused board members to be reluctant to disagree with him.

The performance of the board can be enhanced by identifying the motivating force behind the director's efficiency, the size, and the preeminent mix between executive, independent, non-executive, and non-independent non-executive directors so that the subsequent board will feature a variety of viewpoints considerable formal independence and strong company

¹²⁸⁹ Blount 2016:373.

¹²⁹⁰ https://www.usb.ac.za/usb_insights/the-steinhoff-scandal-why-due-diligence-alerts-matter/ Accessed 30/06/2022.

¹²⁹¹ Tung 2011:1176.

¹²⁹² Tung 2011:1185.

and industrial understanding. The primary, independent point of reference for board membership¹²⁹³ only considers a director's affiliation with the company. Sharpe has denoted this sort of independence¹²⁹⁴ as "cosmetic independence." Sharpe¹²⁹⁵ proposes that an additional essential methodology to independence is required wherein the "cosmetic independence" approach is replaced by a "substantive methodology" for selecting directors. The substantive methodology consists of the components of time, information and knowledge required for a board to make well-informed resolutions, which forms the basis of the board's oversight and monitoring roles. I agree with Sharpe¹²⁹⁶ that the cosmetic independence of corporate boards¹²⁹⁷ has an adverse bearing on the decision-making processes and how the board participates in successfully monitoring management since unaffiliated directors will lack the qualities of time, information and understanding to successfully monitor top management and avoid corporate failure. I believe that in the instance of Steinhoff, members of the board often sat in different committees during the same financial year, thus having a negative impact on the time they'll have to successfully participate in decision monitoring of the board.

A director's independence is frequently inhibited by the social dynamic and fundamental preconceived notion of board meetings and boardroom norms, which confines the director's precarious assessment of the CEO's suggestions.¹²⁹⁸ In addition, a director's independent judgment may be constrained if he feels obligated to support the CEO who nominated his appointment or fears that he will not be reappointed if he voices an opinion contrary to the majority of other board members¹²⁹⁹ or critically assesses the CEO's proposals as was alleged in the Steinhoff collapse.¹³⁰⁰ Millstein argues that previous corporate governance collapses resulted from passive directors who looked the other way while management made poor decisions.¹³⁰¹ Millstein concludes that the key to preventing future corporate governance failures is a fundamental change in corporate leadership. I agree with Millstein that directors and stakeholders must become vigorous competitors

¹²⁹³ Which is both static and decontextualized.

¹²⁹⁴ Sharpe 2011:1435.

¹²⁹⁵ Sharpe 2011:1436.

¹²⁹⁶ Sharpe 2011:1436-1437.

¹²⁹⁷ Corporate boards Sharpe 2011:1436.

¹²⁹⁸ Sharpe 2011:1449.

¹²⁹⁹ Also known as groupthink which limits the board's independence for the purpose of monitoring.

¹³⁰⁰ www.news24.com/fin24/companies/markus-jooste-created-climate-of-fear-former-exec-tells-german-court-20230510 Accessed 11/05/2023.

¹³⁰¹ Millstein 2017:3.

and activists in challenging management decisions and corporate practices.¹³⁰² The board should consist of independent directors who are trusted to make the right decisions and play an important advisory role.¹³⁰³ A director's remuneration should have an equity-based component and be aligned with the directors' and shareholders' interests.

The perception is that good corporate governance principles positively affect a company's performance and attract foreign investment. Ethical leadership is required from the board of directors, and each director should adhere to the duties of a director.¹³⁰⁴ The failure of Steinhoff not only demonstrated the negative impact that the board's failure to adhere to good corporate governance practices had but also the absence of independent directors and their inability to exercise rigorous oversight and accountability had on the company's reputation, share price, and long-term viability.¹³⁰⁵

I am of the opinion in the case of Steinhoff, the failure of the executive team to commit to ethical business practices, in particular with the board that crossed ethical boundaries and was anchored by dominant personalities, caused the company to take enormous financial risks with the rapid acquisitions and profitability drive that was not sustainable. Steinhoff ultimately failed. When shareholders and other stakeholders suffered enormous financial losses, it was abundantly clear that the board had failed in its oversight role to regulate their behaviours and adhere to the values that had been established.

2.2.2 ONGOING EVALUATION

Ongoing evaluation, refining and implementing new corporate governance measures are essential in preventing corporate collapse.¹³⁰⁶ Continuously reviewing corporate governance measures and practices may require significant changes to a company's top management, culture, processes, and decision-making structures. Ongoing efforts to strengthen corporate governance practices may create resistance from employees and managers who are comfortable with the status quo or fear losing power or influence. As

¹³⁰² Millstein 2017:87.

¹³⁰³ Tung 2011:1175.

¹³⁰⁴ Jones 2017:755;Wiese 2018:3.

¹³⁰⁵ Al Shunnaq and Al Azzam 2018:46.

¹³⁰⁶ Cosma 2018:458.

argued by Otsuka, if boards remain passive and do not constantly monitor and evaluate corporate performance based on independent information and not the information solely provided by the CEO, they will not be able to challenge and question the decisions of executives and dominant CEOs to ensure effective board oversight, transparency, accountability and increase the long term wellbeing of the company.¹³⁰⁷ I agree with remarks made by Sharpe and Blount that the decision-making processes that management and boards follow to monitor corporate performance need significant improvement.¹³⁰⁸ The focus should primarily be on how the board monitors corporate performance. Precautionary methods should be flexible, authentic and varied to enable stakeholders to participate voluntarily¹³⁰⁹ and less in the board's regulatory, compositional and structural reforms.¹³¹⁰ I am of the opinion that if the Steinhoff board had been renewed regularly to ensure that new perspectives on corporate governance, its values, mission, vision, and strategy were introduced to management and the board remained independent of the management, the collapse could have been prevented.

2.2.3 EFFECTIVE LEADERSHIP

One of the most important factors in ensuring effective corporate governance is enhanced leadership. In addition to ensuring that the board is competent in providing strategic direction and carrying out its legal and fiduciary responsibilities, the chairman is tasked with overseeing the performance of the executive team. The board must have a sense of direction, and each director must be considered an independent¹³¹¹ competent, consistent, responsible, and honest leader, not just a box ticker. Corporate governance practices require the support and commitment of management to be effective. However, challenges may arise if some leaders may not fully comprehend the importance of corporate governance or the application thereof. This may result in prioritizing short-term financial goals over long-term sustainability and ethical considerations. To ensure that each board member acts in good faith with the necessary care, skill and diligence and within the interest of the company, I concur with the suggestion made by Millstein¹³¹² that each

¹³⁰⁷ Otsuka 2017:72.

¹³⁰⁸ Sharpe 2012:3.

¹³⁰⁹ Blount 2016:417.

¹³¹⁰ Sharpe 2012:4.

¹³¹¹ Directors serving on boards too long are at risk of losing their independence. Botha 2018:1.

¹³¹² Millstein 2017:165.

director should sign an "Acknowledgement of fiduciary duties and responsibilities" reflecting these obligations to ensure that board members exercise their fiduciary duties without being influenced by fear, friendship, or personal gain.

McGregor's proposition is a national strategy that focuses on re-education, training, coaching and mentoring inexperienced directors on fiduciary duties and enforcement of fiduciary duties, regardless of whether such establishment is in the public, private or non-profit sectors.¹³¹³ Both proposals of Millstein and McGregor touched on the critical aspects of the fiduciary duties of directors in ensuring good corporate governance. I concur with Grove, Mac Clouse and Xu's proposed corporate governance benchmark analysis.¹³¹⁴ The board of directors should use the board director benchmarking analysis to assess and compare their own boards' corporate governance practices with the practices of other companies to prevent corporate failure.¹³¹⁵ Benchmarking categories include board comparison,¹³¹⁶ board oversight of risk management, executive misconduct, executive compensation, comprehensive data security and privacy programs to strengthen corporate governance practices and prevent irregular conduct, and financial performance that affects corporate governance.

2.2.4 DELINQUENT DIRECTORS AND DIRECTORS UNDER PROBATION

Section 162 of the Act regulates the application to declare a director delinquent or under probation and applies to a juristic person.¹³¹⁷ Suppose a foreign company is registered as an external company¹³¹⁸ but not subject to certain provisions of the Act. In that case, the laws of its country of incorporation will regulate the appointment and removal of its directors.¹³¹⁹

¹³¹³ Cassim et al 2018:272. McGregor 2011:408.

¹³¹⁴ Grove et al 2020:16-17. Smith 2018:1.

¹³¹⁵ Grove et al 2020:11.

¹³¹⁶ Board size, specific industry knowledge of directors, diversity of directors (gender, age skills), frequency of board meetings, board committees, annual performance assessment of the board, board committee rotation, coaching and mentoring of board members, board leadership. Wiese 2018:26.

¹³¹⁷ In terms of Section 1 of the Act a juristic person includes a foreign company and a trust irrespective of whether or not it was established within or outside the Republic. Wiese 2018:53.

¹³¹⁸ Section 23 (2) of the Act.

¹³¹⁹ Du Plessis and Delport 2017:276.

As stipulated in section 162 (2) of the Act, a company, a shareholder, director, company secretary or prescribed officer of a company, a trade union that represents employees of the company, or another representative of the employees of a company may apply to a court for an order declaring a person delinquent or under probation if the person is a director of that company or, within the 24 months immediately preceding the application, was a director of that company.¹³²⁰

The first reported case on section 162 was *Kukama v Lobelo*,¹³²¹ wherein K and L were equal shareholders in two companies, P (Pty) Ltd and D (Pty) Ltd. K applied for an order to declare L as a delinquent director because L failed in his duty as a director¹³²² to declare to his co-director and the board that a fraudulent claim of R39 million was submitted to SARS.¹³²³ Upon receipt of the fraudulent claim, he willfully failed to refund SARS. This amounted to gross negligence and breach of trust, which caused irreparable harm to the company, and the refund payment was made to other companies¹³²⁴ this caused irreparable harm to P (Pty) Ltd. L breached his fiduciary duties towards P (Pty) Ltd. The court granted the order, and L was declared a delinquent director.

2.2.5 DELINQUENT DIRECTOR

In the context of an application seeking to declare an individual as a delinquent director,¹³²⁵ the court is required to issue an order in cases where an individual has been disqualified while serving as a director, has given consent to act as a director, or has served as a director or prescribed officer while being ineligible or disqualified according to section 69 of the Act.¹³²⁶ Engaging in directorial activities that violated the terms of probation as outlined in section 162 of the Act,¹³²⁷. The declaration of delinquency is characterised by its unconditional nature and remains in effect for the entirety of the individual's lifetime upon being proclaimed delinquent.¹³²⁸

¹³²⁰ Section 162 (2) (a) of the Act. Wiese 2018:53.

¹³²¹ *Lebelo & others v Kukama & others* 2013 ZAGPJHC 72

¹³²² Section 76 (2) (b) of the Act.

¹³²³ South African revenue services

¹³²⁴ Du Plessis and Delpont 2017:285.

¹³²⁵ Section 162 (5) of the Act.

¹³²⁶ Section 162 (5) (a) of the Act.

¹³²⁷ Section 162 (5) (b) of the Act.

¹³²⁸ Section 162 (6) (a) of the Act.

While a director engaged in misconduct by exploiting the position for personal gain,¹³²⁹ which is in violation of section 76 (2) (a) of the Act intentionally or negligently caused harm to the company or one of its subsidiaries, also contravening section 76 (2) (a) of the Act. Furthermore, has repeatedly been personally subject to a compliance notice or similar enforcement mechanism for substantially similar conduct, in terms of any legislation.¹³³⁰

If the individual in question has been convicted of an offence on at least two occasions, or has been subjected to an administrative fine or a comparable penalty, as stipulated by relevant legislation,¹³³¹ or within five years was a director of one or more companies or a managing member of one or more close corporations, or controlled or participated in the control of a juristic person, concurrently, sequentially, or at unrelated times, that were convicted of an offence or subjected to an administrative fine or similar penalty in terms of any legislation,¹³³² and the person was at the time of the contravention that resulted in the conviction, administrative fine or other penalty, a director or managing member of the corporation or close corporation or was responsible for the management of each such juristic person.¹³³³

If the court is satisfied that the declaration of delinquency is justified having regard to the nature of the contraventions and the person's conduct in relation to the management, business or property of any company, close corporation or juristic person at the time the court will grant the application.¹³³⁴

In *Gihwala v Grancy*,¹³³⁵ the appeal court stated that there is a "bond of trust" between shareholders and the directors they elect. The court further confirmed that a declaration of delinquency in terms of section 163 (5) (c) is not unconstitutional and may be made subject

¹³²⁹ Section 162 (5) (c) (i)-(iv) of the Act.

¹³³⁰ Section 162 (5) (d) of the Act. https://www.sabinet.co.za/https://journals.co.za/doi/abs/10.10520/AJA00104051_83 Accessed 12/08/2023.

¹³³¹ Section 162 (5) (e) of the Act. https://www.sabinet.co.za/https://journals.co.za/doi/abs/10.10520/AJA00104051_83 Accessed 12/08/2023

¹³³² Section 162 (5) (f) of the Act. https://www.sabinet.co.za/https://journals.co.za/doi/abs/10.10520/AJA00104051_83 Accessed 12/08/2023

¹³³³ Section 162 (5) (f) (i) of the Act. https://www.sabinet.co.za/https://journals.co.za/doi/abs/10.10520/AJA00104051_83 Accessed 12/08/2023

¹³³⁴ Section 162 (5) (f) (ii) of the Act. https://www.sabinet.co.za/https://journals.co.za/doi/abs/10.10520/AJA00104051_83 Accessed 12/08/2023

¹³³⁵ *Gihwala & others v Grancy Property Ltd & others* 2016 All SA 649 SCA

to any conditions the court considers appropriate, including limiting the application of declaration to one or more particular categories of companies¹³³⁶ and exists for seven years¹³³⁷ from the date of the order, or such longer period as determined by the court at the time of making the declaration subject to subsections (11) and (12).

2.2.6 PROBATION

A court has the authority to grant a probation order¹³³⁸ provided that whilst serving as a director the individual was in attendance at a meeting when a resolution was put forth, and notwithstanding the company's failure to meet the solvency and liquidity criteria as stipulated by the Act, refrained from voting against said resolution.¹³³⁹ If the individual otherwise acted in a manner that was fundamentally contradictory to the responsibilities of a director¹³⁴⁰ or acted in or supported a decision¹³⁴¹ of the company to act in a manner contemplated in section 163 (1) or refrain from holding such positions within a span of 10 years following the effective date, this restriction applies regardless of whether the individual has served as a director for multiple companies or as a managing member for multiple close corporations, whether simultaneously, consecutively, or at separate instances.¹³⁴² and during that time the person was a director of each such company or managing member of each such close corporation, two or more of those companies or close corporations each failed to fully pay all of its creditors or meet all of its obligations, except in terms of a business rescue plan¹³⁴³ resulting from a resolution of the board in terms of section 129 of the Act or a compromise with creditors.¹³⁴⁴

The court possesses discretionary authority to issue a declaration that places an individual on probation, with the imposition of conditions deemed suitable by the court. These requirements may include limitations on the scope of the declaration, restricting its application to specific categories of corporations.¹³⁴⁵

¹³³⁶ Section 162 (6) (b) (i) of the Act.

¹³³⁷ Section 162 (6) (b) (ii) of the Act.

¹³³⁸ Section 162 (7) (a)-(b) of the Act.

¹³³⁹ Section 162 (7) (a)-(i) of the Act.

¹³⁴⁰ Section 162 (7) (a)-(ii) of the Act.

¹³⁴¹ Section 162 (7) (a)-(iii) of the Act.

¹³⁴² Section 162 (7) (b)-(i) of the Act.

¹³⁴³ Section 162 (7) (b)-(ii) (aa) of the Act.

¹³⁴⁴ Section 162 (7) (b)-(ii) (bb) of the Act.

¹³⁴⁵ Section 162 (9) (a) of the Act.

Without limiting the powers of the court, the court may order as conditions applicable or ancillary to a declaration of delinquency or probation that the person concerned to undertake a designated programme of remedial education¹³⁴⁶ relevant to the nature of the person's conduct as a director,¹³⁴⁷ carry out a designated programme of community service;¹³⁴⁸ pay compensation to any individual who has suffered negative consequences as a result of the director's actions, particularly in cases when the aggrieved party lacks alternative legitimate reasons for seeking compensation.¹³⁴⁹

In the case of an order of probation be supervised by a mentor¹³⁵⁰ in any future participation as a director while the order remains in force,¹³⁵¹ or be limited to serving as a director of a private company or of a company of which that person is the sole shareholder.¹³⁵²

2.3 EMPLOYEE SHAREHOLDER AND STAKEHOLDERS' RIGHTS AND POWERS

It is essential for employees to be involved in the decision-making process if they are to effectively oversee management and participate in corporate governance in their capacity as shareholders.¹³⁵³

Different mechanisms are utilised to ensure employees' participation in corporate governance.¹³⁵⁴ Board-level participation provides employees the opportunity to obtain information and engage in corporate decision-making through their permanent representatives on the boards. The platform facilitates effective communication between the board of directors and the CEO, while also creating avenues for employees to engage in discussions regarding alternative company strategies aimed at ensuring long-term financial stability.¹³⁵⁵

¹³⁴⁶ The programs and the implementation thereof are not specified.

¹³⁴⁷ Section 162 (10) (a) of the Act.

¹³⁴⁸ Section 162 (10) (b) of the Act.

¹³⁴⁹ Section 162 (10) (c) of the Act.

¹³⁵⁰ The supervisory duties of a mentor are not stipulated the Act.

¹³⁵¹ Section 162 (10) (d) (i) of the Act.

¹³⁵² Section 162 (10) (d) (ii) of the Act.

¹³⁵³ See Clarke 2005:339-370 state that for example in Japan workers participate management decisions and this relationship is referred to as a relational corporate governance system.

¹³⁵⁴ Sefara 2019:20.

¹³⁵⁵ Sefara 2019:19.

2.3.1 SHAREHOLDER PARTICIPATION AND ACTIVISM

Shareholders are individuals or organisations with a financial stake in a company. Examples of shareholders are individuals, directors, employees, customers, the community, the government, business partners, the media, and creditors. Shareholders might be either individual or institutional investors. They may consist of business associations, social activists, or labour unions. A beneficial interest can be direct or indirect. In addition to preference and control, shareholders can also be classified as majority and minority shareholders.

Shareholder activism is one of the concerns related to corporate governance that the management and board of directors of each corporation must carefully consider to successfully implement corporate governance practises in their organisations.¹³⁵⁶ It is a method by which investors express their concerns or dissatisfaction with the corporations they have invested in.¹³⁵⁷ If companies do not comply with corporate governance guidelines, they may face shareholder activism.¹³⁵⁸ Activism on the part of shareholders involves shareholders taking action or getting involved by posing questions to management, demanding that they be held accountable, and making suggestions to management.¹³⁵⁹ It refers to the methods used by shareholders to influence the behaviour and decisions of a corporation in which they have shares. It involves shareholders using their ownership rights and privileges to advocate for company-wide changes, typically in corporate governance, executive compensation, social and environmental policies, and overall business strategy. This phenomenon began centuries ago but gained momentum and developed in the United States during the 1930s following the 1929 collapse of Wall Street. It quickly spread to countries such as the United Kingdom and the rest of the world.¹³⁶⁰

In section 165 of the Act, a shareholder or trade union may demand that a company institute proceedings or continue with proceedings to protect the company's legal

¹³⁵⁶ Michie and Oughton 2005:517-519.

¹³⁵⁷ www.investopedia.com/terms/s/shareholderactivism.asp Accessed 22/04/2021.

¹³⁵⁸ Lekhesa 2009:25.

¹³⁵⁹ Beebeejaun and Koobloll 2018:1425-1426;Lekhesa 2009:10-15.

¹³⁶⁰ Lekhesa 2009:12.

interests.¹³⁶¹ Shareholders may claim damages when a person has intentionally or due to gross negligence or fraudulently caused the company to act inconsistently with the Act.¹³⁶² Viviers¹³⁶³ defines shareholder activists as investors who use their equity stake in the investee companies to consult with management on issues that affect their shareholder value and demand corporate accountability.¹³⁶⁴ The general meeting (collective shareholders) and the board of directors are the main organs of a company. Section 66 (1) of the Act creates a positive duty on the board of directors to manage the business and affairs of the company and gives the authority to exercise all of the powers and perform any of the functions of the company except to the extent that the Act or MOI states otherwise. It is during these annual general meetings that individual or institutional shareholder activists (irrespective of whether they are financially,¹³⁶⁵ socially¹³⁶⁶ or non-financially¹³⁶⁷ motivated) need to become more assertive and confrontational regarding poor corporate governance issues and persistent in their engagement and use deadlines to ensure urgent responses are received from the investee companies.¹³⁶⁸ The impact of shareholder activism is contingent on the method of activism and the nature of shareholder demands. As negative publicity can be detrimental to business, shareholder pressure on matters that could cast a negative light on a company is likely to produce the desired result. The threat of or actual negative publicity can encourage a company to reconsider its policies, particularly if public opinion is against the practice. Companies can still employ the "comply and explain" principle of corporate governance to fend off activist shareholders.¹³⁶⁹

The board of directors has the ultimate power and responsibility for good corporate governance. Directors owe fiduciary duties to the company and cannot transfer their duties to the shareholders. Directors can transfer their powers to the shareholders or anyone

¹³⁶¹ Calkoen 2020:284.

¹³⁶² Calkoen 2020:283.

¹³⁶³ Viviers 2016:348.

¹³⁶⁴ Zhao and Wen 2022:77-78; Beebeejaun and Koobloll 2018:1425.

¹³⁶⁵ Focuses on financial accounting such as reducing expenses and increase dividend pay-outs.

¹³⁶⁶ Focuses on creating a just and sustainable society and human rights.

¹³⁶⁷ Focuses on public companies' compliance with corporate governance and governance irregularities. Zhao and Wen 2022:82-83.

¹³⁶⁸ Viviers 2016:351.

¹³⁶⁹ Lekhesa 2009:166.

else.¹³⁷⁰ In *De Bruyn vs Steinhoff International Holdings NV and others*,¹³⁷¹ the Gauteng High Court had to determine if directors or external auditors owed any duty of care to existing and prospective shareholders and in terms of the common law and section 218 (2) of the Act can be held liable for the financial losses caused by financial misstatements (the income and assets of the Steinhoff companies were overstated and the liabilities of these companies were understated).

In *Howard v Herrigal and Another NO*¹³⁷² the Appeal court confirmed that in terms of the common law, by virtue of accepting an appointment as director, the relevant person becomes a fiduciary in relation to the company and, as such, is expected to exhibit the utmost good faith towards the company in all that he/she does on behalf of the company. The fiduciary duties form part and parcel of the characteristics of a director and cannot be ignored or avoided. The court confirmed that in terms of the common law, there is no general fiduciary duty owed by directors to shareholders of the company. A "special factual relationship" between the shareholder and company¹³⁷³ is required to prove the existence of a fiduciary duty between a director and shareholders.¹³⁷⁴ Usually, a special factual relationship requires a personal relationship between shareholders and directors or some specific transactions between directors and shareholders.¹³⁷⁵ Notably, the court noted that Steinhoff was not a small company as opposed to a family business with closely held shares, and thus the directors were not liable to shareholders or potential shareholders for the loss in share value.¹³⁷⁶

¹³⁷⁰ Esser and Delport 2017:225.

¹³⁷¹ *De Bruyn v Steinhoff International Holdings NV and others* 2022 (1) SA 44 (GJ) 442. Honourable Judge Unterhalter remarked that it is generally accepted that the legal relationship between a director and a company does not give rise to fiduciary duties owed to the company's shareholders or any other third party, such as a creditor. Matshebala 2022 <https://www.werksmans.com/legal-updates-and-opinions/and-we-dare-to-ask-again-whose-right-is-it-to-enforce-a-directors-fiduciary-duties-the-company-or-the-creditors> Accessed 15/6/2023.

¹³⁷² *Howard v Herrigal and Another NO* 1991 (2) SA 660 (A).

¹³⁷³ Individually or collectively. Zhao and Wen 2022:73.

¹³⁷⁴ Mashige ea 2020:9. *Ryan and Others vs Groenendaal and Others* 2022 ZAGPJHC 309, the court found that a director may owe fiduciary to someone other than the company should a special factual relationship exist.

¹³⁷⁵ Matshebala 2022 <https://www.werksmans.com/legal-updates-and-opinions/and-we-dare-to-ask-again-whose-right-is-it-to-enforce-a-directors-fiduciary-duties-the-company-or-the-creditors> Accessed 15/6/2023.

¹³⁷⁶ *De Bruyn v Steinhoff International Holdings NV and others* 2022 (1) SA 44 (GJ) 443. Zhao and Wen 2022:73.

An important feature of corporate governance is proactive shareholder engagement, responsible stewardship and collaborative engagement between shareholders and listed companies.¹³⁷⁷ Shareholders and stakeholders must scrutinise annual reports and hold board members accountable for the company's performance.¹³⁷⁸ I believe that active shareholder participation could have prevented the negative effect the collapse of Steinhoff had on both individual and institutional investors that include public pension funds and private equity funds.

2.4 TRANSPARENCY

Former US Supreme Court Justice Louis Brandeis described the importance of transparency as "sunlight is the best disinfectant",¹³⁷⁹ as quoted by Wong.¹³⁸⁰ The foremost objective of transparency is ensuring adequate and unvarying information¹³⁸¹ is timeously divulged to stakeholders and shareholders to make informed investment conclusions. Transparency guarantees equal access to information between management and shareholders reassures preferred behaviour, and manages potential conflicts of interest among parties.¹³⁸²

Zhao and Wen emphasized that in the context of corporate governance, the board is accountable to shareholders and stakeholders to provide accurate information, thereby ensuring transparency.¹³⁸³ In terms of time and expenses, published information can become relatively expensive. Compulsory areas for disclosure should be selected to prevent the publication of superfluous, less beneficial information. New compulsory areas for disclosure should be selected, and less pertinent subjects should be disregarded.¹³⁸⁴ Accountability is the most important aspect of corporate governance; the board must justify and explain its decisions. Directors are responsible for overseeing operations and ensuring that required disclosures are made and reports regarding board decisions are accurate.

¹³⁷⁷ Zhao and Wen 2022:77-78.

¹³⁷⁸ Wong 2009:6.

¹³⁷⁹ Delpont 2005:388. Al Shunnaq and Al Azzam 2018:45.

¹³⁸⁰ Wong 2009:2.

¹³⁸¹ Corporate performance, sustainability, operational results, financial health, strategy, prospects and risks. Zhao and Wen 2022:76-77.

¹³⁸² Wong 2009:3.

¹³⁸³ Zhao and Wen 2022:77-78.

¹³⁸⁴ Al Shunnaq and Al Azzam 2018:46.

The board must guarantee the legitimacy of all decisions made. In addition, corporate governance includes the imposition of consequences for directors. These consequences may be positive or negative. Positive consequences include promotions or incentive bonuses for corporate achievements or success, and negative consequences such as the removal of a director from the board or the decision not to re-elect a director when their term comes to an end.¹³⁸⁵

In the occurrence of Steinhoff, even if the annual and integrated reports can be considered "best practice", there was a discrepancy between the content of the annual and integrated reports and the alleged performance reported. There was a difference between the reporting practices and those in the reported company.¹³⁸⁶

Transparency does not at all times attain its anticipated objective, as it is unmistakably exemplified in the Steinhoff 2011 corporate governance report:

"Steinhoff has not established a formal process of obtaining assurance on ethical awareness and ethical compliance throughout the group."¹³⁸⁷

As a result of the lack of transparency, investors lost confidence in the reliability of the divulged information, leading to substantial monetary losses.

2.5 SOCIAL AND ETHICS COMMITTEE

The social and ethics committee (hereafter "SEC") is entitled¹³⁸⁸ to any information or explanation at any general stakeholders meeting necessary to report on its mandate to shareholders at the company's annual general meeting.¹³⁸⁹ In terms of Regulation 43 (5) of the Act, the functions of the SEC include monitoring the company's activities with regard to social and economic development, good corporate citizenship, the environment, health and safety, consumer relationships and labour and employment.¹³⁹⁰ The biggest challenge

¹³⁸⁵ Zhao and Wen 2022:78-79.

¹³⁸⁶ Naude et al 2018:8.

¹³⁸⁷ Corporate governance report 2011:83.

¹³⁸⁸ Esser and Delpont 2017:222.

¹³⁸⁹ Regulation 43 (3).

¹³⁹⁰ Wiese 2018:44-45.

in terms of Regulation 43 (5) (c) of the Act is the SEC (regarded as a company committee) must act in the best interest of the company. In contrast with the board committee, the SEC has no fiduciary duties regarding the common law or any other act towards the company.¹³⁹¹

The SEC may bring any matter within its mandate to the board's attention and report it to the shareholders. If the recommendation to the board is not approved, such a recommendation cannot be implemented.¹³⁹² The SEC will report back to the general meeting of shareholders on the outcome of the recommendation. Esser and Delpont¹³⁹³ state that shareholders have the ultimate power to remove a specific director or all the directors and can determine the board's structure, which could affect the board's discretion regarding implementing recommendations made by the SEC. From a corporate governance perspective, it is obvious to ask where the SEC was in assuring ethical awareness and ethical compliance amongst staff, particularly the board of directors and management. In fulfilling its mandate, what steps did the SEC take to monitor Steinhoff's alleged accounting irregularities-related activities? I suggest that the mandate of the SEC be enlarged to include oversight in financial and regulatory compliance matters.

2.6. AUDIT COMMITTEE

The complexity of corporate structures and the complexity level of acquisitions may result in the failure of the audit committee to ensure accurate reporting, transparency, and adequate oversight. An independent director should be the chairperson of the audit committee. The audit and risk committee should be separate, and training for members of the committees be mandatory. The rotation of auditors is compulsory. The company must elect the audit committee and not the board of directors at each public company's annual general meeting. The audit committee should comprise may be of a minimum of three directors who are not prescribed officers or involved in the daily management of the company or full-time executive employees of the company, inter-related company,

¹³⁹¹ Esser and Delpont 2017:230.

¹³⁹² Delpont 2011:89.

¹³⁹³ Esser and Delpont 2017:231.

or another related company.¹³⁹⁴ I believe that an independent audit committee contributes to preventing fraud but cannot prevent all fraudulent accounting practices. Audit committees do not meet frequently enough to prevent every instance of accounting fraud. I concur with Beecher- Monas¹³⁹⁵ that the relationship between the board and management, and external auditors have an adverse impact on the audit committee's work, as the management can influence the interaction between the audit committee and external auditors. The number of independent directors must outweigh the other directors' influence. Nonetheless, independent directors will rely heavily on information provided by the board, particularly the chief executive officer, chief financial officer, chairman of the board, and other directors and officers. Also problematic is when the board disregards the audit committee's advice or information regarding concerns within the company, such as fraudulent accounting practices. Linked to this issue is that external auditors may find it laborious to detect fraud in audited financial reports. In the instance of Steinhoff, the minimal compliance, lack of insight into financial statements and commitment to sound corporate governance practices to satisfy the relevant authorities and shareholders leads to mediocrity and compliance being a mere "tick box" exercise.¹³⁹⁶ I believe that the dubious financial practices that are currently being investigated, deception and weak accountability, should have raised more questions from shareholders and stakeholders.

2.7 ROTATION OF AUDITING FIRMS

As prescribed by the independent regulatory board of auditors,¹³⁹⁷ the mandatory rotation of auditing firms for public interest entities and compulsory training for audit committees should be mandatory and included in future legislation.

2.8 JOHANNESBURG STOCK EXCHANGE (JSE) LISTING REQUIREMENTS

The purpose of the JSE Listing requirements is to ensure that the business of the JSE is carried on with due regard to the public interest. All companies (including securities issued

¹³⁹⁴ Delpont 2011:123.

¹³⁹⁵ Beecher-Monas:2007:379.

¹³⁹⁶ <https://www.wits.ac.za/news/latest-news/in-their-own-words/2018/2018-04/steinhoffs-board-behaved-badly-and-should-be-held-account.html> Accessed 09/03/2019.

¹³⁹⁷ Hereafter the IRBA

by companies, foreign or domestic) listed on the JSE need to fulfil those requirements to have their shares listed on the Johannesburg stock exchange.¹³⁹⁸ In response to the corporate scandals of 2017 and 2018 in the South African markets, the JSE announced the amendment of its listing requirements.¹³⁹⁹ The objective was to improve the standard of corporate governance, enhance the level of disclosures by listed companies and improve the credibility of financial information, thereby protecting investors and ensuring investors can make informed investment decisions.

Paragraph 3.84¹⁴⁰⁰ of the listing requirements states that issuers¹⁴⁰¹ must implement specific corporate governance practices and disclose compliance in their annual reports.¹⁴⁰² To ensure a clear balance of power and authority, there must be evidence (in the form of a policy) that no director has unlimited decision-making powers.¹⁴⁰³ The same person must not hold the chief executive officer and chairperson positions. In accordance with the King Code, the chairperson must be either an independent non-executive director or a lead independent director. Following the King Code, the following committees must be appointed an audit committee, a remuneration committee and a social and ethics committee.¹⁴⁰⁴ The compliance of each committee must be in accordance with the Act and the recommended practices in the King Code on an apply and explain basis.¹⁴⁰⁵ Each committee must comprise of a minimum of three members.¹⁴⁰⁶ An abbreviated CV of each director in respect of a new listing or a director standing for election or re-election at a general meeting or the annual general meeting should accompany the notice of the general meeting or annual general meeting;¹⁴⁰⁷ Each director must be categorised as

¹³⁹⁸ JSE Listing requirements. [Service Issue 27_1.pdf \(jse.co.za\)](#) Accessed 28/7/2022.

¹³⁹⁹ <https://www.jse.co.za/news/press-releases/jse-announces-amendments-listing-requirements-strengthen-primary-and-secondary> Accessed 28/7/2022.

¹⁴⁰⁰ p48.

¹⁴⁰¹ Issuers include any company excluding an issuer of specialist securities and any class of whose securities has been admitted p11.

¹⁴⁰² The application of the corporate governance practices in the King Code is voluntarily the effect of incorporating certain practices from the King Code in the Listings Requirements is to make their implementation mandatory.

¹⁴⁰³ Paragraph 3.84 (a).

¹⁴⁰⁴ Paragraph 3.84 (c).

¹⁴⁰⁵ A brief description of the committees' mandates the number of meetings held and other relevant information must be disclosed in the annual report.

¹⁴⁰⁶ Paragraph 3.84 (d).

¹⁴⁰⁷ Paragraph 3.84 (e).

executive,¹⁴⁰⁸ non-executive¹⁴⁰⁹ or independent.¹⁴¹⁰ An executive financial director must be appointed for all companies.¹⁴¹¹

The Audit Committee may request¹⁴¹² the JSE to allow the appointment of a financial director on a part-time basis. The JSE may, after considering the special request, allow the employment of the financial director on a part-time basis or refuse the appointment.¹⁴¹³ In terms of Section 94 of the Act, the audit committee's annual functions include annually considering the appropriateness of the experience and expertise of the financial director,¹⁴¹⁴ ensuring that functional financial reporting procedures are established¹⁴¹⁵ to ensure that access is allowed to all the financial information of the issuer to allow the issuer to effectively prepare and report on the financial statements of the issuer.¹⁴¹⁶ The audit committee must request from the audit firm detailed information¹⁴¹⁷ of their assessment of the suitability for appointment of their current or a prospective audit firm and designated individual partner both when they are appointed for the first time and after that annually for every re-appointment as well as for an applicant issuer before listing,¹⁴¹⁸ and notwithstanding the provisions of section 90(6) of Act. As per section 61 (8) of the Act, the appointment of the auditor must be presented as a resolution included at the annual general meeting. The issuer must report in its annual report to the shareholders that the audit committee has executive responsibilities as stipulated in paragraph 3.84 (g) of the JSE listing requirements.

Companies must appoint a company secretary in accordance with the JSE listing requirements¹⁴¹⁹ and the Act. The recommended practices in the King Code should be

¹⁴⁰⁸ Executive directors are involved in the management of the company and/or in full-time salaried employment of the company and/or any of its subsidiaries.

¹⁴⁰⁹ Non-executive directors are part time directors who are not involved in the day to day management of the company, or full-time salaried employees of the company and/or any of its subsidiaries. Non-executive directors are usually appointed to the board of directors to provide independent and objective judgment to the management

¹⁴¹⁰ Independent directors do not have any relationship with the company outside their directorship that could interfere with their independent judgment of the company.

¹⁴¹¹ Paragraph 3.84 (f).

¹⁴¹² Special permission due to special circumstances, accompanied by a detailed motivation.

¹⁴¹³ Paragraph 3.84 (g).

¹⁴¹⁴ Paragraph 3.84 (g) (i).

¹⁴¹⁵ Paragraph 3.84 (g) (ii).

¹⁴¹⁶ Paragraph 3.84 (g) (ii).

¹⁴¹⁷ The information as detailed in paragraph 22.15(h).

¹⁴¹⁸ Paragraph 3.84 (g) (iv).

¹⁴¹⁹ Paragraph 3.84 (h).

applied. The board of directors must confirm in its annual report to shareholders that it considered the experience, competence and qualifications in appointing the company secretary.¹⁴²⁰ The nomination committee, or the board of directors, must apply the policy of broad diversity in the nomination and appointment of directors.¹⁴²¹ Suppose any of the diversity indicators have not been applied. In that case, the board of directors or the nomination committee must provide reasons and report progress made on agreed voluntary targets.

At the annual general meeting, the remuneration policy and the implementation report must be tabled by the issuer for separate non-binding advisory votes by the shareholders.¹⁴²² Suppose either or both the remuneration policy or the implementation report are voted against by shareholders exercising 25% or more. In that case, it must be recorded in the remuneration policy and the measures that the issuer's board of directors commits to. To give effect to the minimum measures referred to in the King Code, the issuer must, in its voting results, announce paragraph 3.91 and invite dissenting shareholders to meet with the issuer¹⁴²³ and the timing and manner of the engagement.¹⁴²⁴

After due, careful and proper consideration, a responsibility statement must be made by the CEO and the financial director confirming that the directors, whose names are stated, confirm that the annual financial statements, in all material respects, fairly present the financial performance, financial position and cash flows of the issuer in terms of IFRS;¹⁴²⁵ that no facts have been omitted or untrue statements made that would make the annual financial statements misleading or false;¹⁴²⁶ to ensure effective preparation of the financial statements, internal financial controls have been put in place to ensure that material information relating to the issuer and its consolidated subsidiaries have been provided¹⁴²⁷ and internal financial controls are effective, adequate and can be relied upon in compiling the annual financial statements, having fulfilled our role and function within the combined

¹⁴²⁰ Paragraph 3.84 (i).

¹⁴²¹ Focusing on the specific promotion of the diversity attributes of race, gender, age, culture, skill, field of knowledge, experience.

¹⁴²² Paragraph 3.84 (j).

¹⁴²³ Paragraph 3.84 (j) (a).

¹⁴²⁴ Paragraph 3.84 (j) (b).

¹⁴²⁵ Paragraph 3.84 (k) (i) (a).

¹⁴²⁶ Paragraph 3.84 (k) (i) (b).

¹⁴²⁷ Paragraph 3.84 (k) (i) (c).

assurance model under principle 15 of the King Code. The CEO and financial director confirm in writing:

*"Where we are not satisfied, we have disclosed to the audit committee and the auditors the deficiencies in design and operational effectiveness of the internal financial controls and any fraud that involves directors, and have taken the necessary remedial action".*¹⁴²⁸

During 2022, the JSE conducted investigations against Jooste relating to failure to comply with accounting standards and JSE listing requirements and publishing materially false and misleading information. Jooste was found guilty and received two public censures and two "maximum permissible" fines for Steinhoff's 2015, 2016 and prior year financial statements that did not comply with accounting standards and the JSE listings requirements.¹⁴²⁹ I am of the opinion that JSE listing requirements should be revised to include expanded powers for companies with primary international listings, compulsory training of audit committees, regulatory oversight on directors' dealing and regulatory oversight on secondary listings.¹⁴³⁰

3. DUE DILIGENCE SCREENING GUIDELINES

To determine a company's financial standing, precautionary procedures can be employed. As stated by Malan,¹⁴³¹ the following due diligence screening guidelines and follow-up procedures were applied to evaluate Steinhoff International Holdings' financial standing from 2013 to 2016, and the following conclusions were reached:¹⁴³²

¹⁴²⁸ Paragraph 3.84 (k) (i) (d).

¹⁴²⁹ <https://www.iol.co.za/business-report/companies/tribunal-is-considering-the-jses-fines-against-former-steinhoff-ceo-markus-jooste-345e7f99-4b0f-4a35-8afb-f295c287a5dc> Accessed 23/06/2023.

¹⁴³⁰ <https://www.moneyweb.co.za/news/companies-and-deals/steinhoff-scandal-a-three-bucket-wonder> Accessed 30/08/2018.

¹⁴³¹ Grove, Clouse and Malan applied due diligence guidelines, fraud models and red flag ratios to Steinhoff International during the fraud period 2013 to 2016, to pick up on alerts. https://www.usb.ac.za/usb_insights/the-steinhoff-scandal-why-due-diligence-alerts-matter/ Accessed 30/06/2022.

¹⁴³² The due diligence screening guidelines were developed by Dan Sierra, chief investment officer of American billionaire businessman John Malone.

- a. To determine whether there were any predictions of fraudulent financial reporting, the Dechow's New Fraud Model was applied. The model applied over the four years predicted fraud at 50%.
- b. To check whether the New Fraud Model's predictions were consistent, the Beneish Old Fraud Model was applied. The results were slightly similar.
- c. The number one manipulator in fraudulent financial statements is revenue recognition.¹⁴³³ The Schilit Quality of Revenues ratio was calculated. This ratio showed red flags 100% of the time for the four Steinhoff reporting periods.
- d. To determine whether cash was being generated from business operations, the Schilit Quality of Earnings ratio was calculated. This ratio indicated red flags only 25% of the time for the four reporting periods.
- e. The Days Sales Receivable Index (DSRI) and Sales Growth Index (SGI) were calculated because of the red flags for quality of revenue. No red flags were indicated with the DSRI. Positive and probable red flags 75% of the time for the four reporting periods were indicated by the SGI.
- f. To determine if the company was generating sufficient cash to survive, the Altman Bankruptcy Model was applied. This index strongly predicted bankruptcy over all four years.
- g. The Sloan Accrual ratio and the total liabilities to stockholder equity ratio were applied to detect red flags for fraud and operating problems. The Sloan Accrual emerged as a huge red flag in 2016 and 2014. Solvency red flags for all four years were indicated by the total liabilities to stockholder equity ratio.
- h. The cash conversion cycle was applied. Red flags were shown for all four years, indicating a dangerous reliance on vendors to help finance Steinhoff's working capital.

¹⁴³³ Revenue recognition is the starting point for cash flow generation by business operations.

Malan¹⁴³⁴ noted that over the course of four years, 64 potential red flags were identified based on the screening guidelines. If a sufficient number of red flags are identified, the analysis must be expanded, and subsequent procedures must be implemented. Malan¹⁴³⁵ stated that, based on the filtering guidelines, procedures for ensuring due diligence were developed. These subsequent actions included;

- a. Competitive analyses of profitability: "If a story is too good to be true"
- b. Competitive analyses of liquidity and solvency: "Management can overcome every major business problem, except running out of cash."
- c. Additional revenue work: This includes looking for "massaged revenue recognition" Site visits and online visits: This is to determine, among others, if third-party contractors are not simply different subsidiaries of the company being investigated – i.e. if phantom accounts have not been created.
- d. Corporate governance and ethics: This includes looking at the ethics of top management, toxic company culture, and board independence.

Corporate governance principles must be reviewed regularly using a Fuzzy Expert System (FES). This rating system measures and manages qualitative data to improve the understanding of both managers and boards of contemporary corporate governance issues and applications.

Finch emphasized that the actual implementation of precautionary processes demands several requirements.¹⁴³⁶ Firstly new rules to demand more detailed reports from the board and by creating an entitlement on the part of the shareholder to demand an independent management consultancy report on a specific topic will enable shareholders, creditors, government departments or agencies to high levels of information, expertise and the ability

¹⁴³⁴ https://www.usb.ac.za/usb_insights/the-steinhoff-scandal-why-due-diligence-alerts-matter/ Accessed 31/08/2022.

¹⁴³⁵ https://www.usb.ac.za/usb_insights/the-steinhoff-scandal-why-due-diligence-alerts-matter/ Accessed 31/08/2022.

¹⁴³⁶ Finch 1992:214.

to deliver if they are to act positively in the case of incompetence.¹⁴³⁷ In fact, Fairfax acknowledges that there is a radical departure from the traditional corporate governance norm of shareholder passivity. Moreover, public company shareholders have begun to increase their voting power against management preferences and influence over director elections.¹⁴³⁸ There is a significant distinction between the United States corporate governance system of implementing a strictly rules-based approach and the European principles-based approach. Another option is adopting a middle road between the two approaches.¹⁴³⁹ South Africa should avoid Germany's mistake of fusing existing legislation with suggestions. This creates uncertainty for investors.¹⁴⁴⁰

I concur with Krackhardt that a compromise must be reached in the case of South Africa between the implementation of new legislation or codes to prevent corporate governance collapses and the financial burden of imposing superfluous rules and codes on local and international companies.¹⁴⁴¹

4. WHISTLE-BLOWING

The main objective of a whistle-blowing policy is to encourage employees to report irregularities and uncover fraud.¹⁴⁴² Under the Protected Disclosures Act¹⁴⁴³ (hereafter the "PDA"), employees are protected against victimisation or any "occupational detriment" when they make certain disclosures of unlawful or irregular conduct of employers or fellow employees. In addition to the PDA, section 159 of the Act provides safeguards against civil, criminal or administrative liability to company stakeholders, shareholders, directors and employees who make disclosures in good faith of specific wrongful or unlawful acts of a company, director or prescribed officers.¹⁴⁴⁴

5. CLAWBACK CLAUSES

¹⁴³⁷ Zhao and Wen 2022:77-78.

¹⁴³⁸ Fairfax 2019:1301;Zhao and Wen 2022:80-81.

¹⁴³⁹ Krackhardt 2005:330.

¹⁴⁴⁰ Krackhardt 2005:357.

¹⁴⁴¹ Krackhardt 2005:357.

¹⁴⁴² Majmudar 2021:85 a similar policy exists in India with the key objective to prevent fraud and to strengthen regulatory measures.

¹⁴⁴³ 26 of 2000.

¹⁴⁴⁴ Calkoen 2020:283;Majmudar 2021:85.

Applying the clawback clause¹⁴⁴⁵ could be a preventive and punitive measure to prevent executives from making questionable decisions.¹⁴⁴⁶ As defined by the Corporate Finance Institute:

*"Clawback is a penalty clause contained in written contracts to prevent managers from using incorrect accounting information, under the clawback provision, the company can request the CEO to pay back the bonus amount previously paid out to the CEO and depending on the specific clawback clause the CEO may also have to return shares and pay a penalty because the original financial reports submitted were flawed."*¹⁴⁴⁷

In recent years, the number of clawback applications has increased due to poor corporate governance practises that led to the payment of CEO incentive compensation in instances where financial reports were flawed. In 2018 Eskom applied to the National Energy Regulator of SA (NERSA) for a regulatory clearing account to recover the R666,6 million it spent above the price estimates of NERSA.¹⁴⁴⁸ Applying clawbacks may have an adverse effect; for example, in the case of Mediclinic, where 58,5% of the minority shareholders voted against the pay resolutions, the executive had been replaced, and 70% of the shares' value had already been destroyed.¹⁴⁴⁹ Clawback clauses must be clearly defined in employment contracts as stipulated under section 34 (1)-(5) of the Basic Conditions of Employment Act.¹⁴⁵⁰

¹⁴⁴⁵ Allows for the recovering of bonuses paid to executives who have overseen corporate failures.

¹⁴⁴⁶ Crotty 2019:2.

¹⁴⁴⁷ <https://corporatefinanceinstitute.com/resources/knowledge/finance/clawback> Accessed 07/06/2022.

¹⁴⁴⁸ Mabuza 2018:1.

¹⁴⁴⁹ Crotty 2019:3.

¹⁴⁵⁰ Basic Conditions of Employment Act 75 of 1997.

Deductions and other acts concerning remuneration

34.(1) An employer may not make any deduction from an employee's remuneration unless—

- (a) subject to subsection (2), the employee in writing agrees to the deduction in respect of a debt specified in the agreement; or
 - (b) the deduction is required or permitted in terms of a law, collective agreement, court order or arbitration award.
- (2) A deduction in terms of subsection (1)(a) may be made to reimburse an employer for loss or damage only if—
- (a) the loss or damage occurred in the course of employment and was due to the fault of the employee;
 - (b) the employer has followed a fair procedure and has given the employee a reasonable opportunity to show why the deductions should not be made;
 - (c) the total amount of the debt does not exceed the actual amount of the loss or damage; and

MTN and Steinhoff illustrate the difficulty in recovering clawback clauses that have not yet been tested in South African courts. However, in 2019 Steinhoff lodged an application against Jooste¹⁴⁵¹ and La Grange¹⁴⁵² to return all bonuses paid to them. The legal action instituted against Steinhoff is expected to take years to finalise. However, it has a useful psychological preventative impact.¹⁴⁵³

6. INVESTIGATIONS INTO STATE-OWNED ENTERPRISES

6.1 PUBLIC INVESTMENT CORPORATION

In 2018 the President of the Republic of South Africa, President Cyril Ramaphosa, appointed a commission of inquiry ("Lex Mpati commission of enquiry") into allegations of impropriety regarding the Public Investment Corporation ("PIC").¹⁴⁵⁴ The PIC manages pension savings belonging to retired government employees on behalf of the Government employees' pension fund. The national treasury has instructed PIC¹⁴⁵⁵ to withhold the payment of incentive bonuses to managers and executives pending the outcome of Judge Lex Mpati commission of inquiry that took place in 2019 to determine who may have been responsible for the collapse of governance at the PIC.¹⁴⁵⁶

In 2020 the Lex Mpati judicial commission commenced with an enquiry into the collapse of governance of the PIC and found that the previous CEO, Dan Matjila, was breaching his

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- (d) the total deductions from the employee's remuneration in terms of this subsection do not exceed one-quarter of the employee's remuneration in money.
 - (3) A deduction in terms of subsection (1)(a) in respect of any goods purchased by the employee must specify the nature and quantity of the goods.
 - (4) An employer who deducts an amount from an employee's remuneration in terms of subsection (1) for payment to another person must pay the amount to the person in accordance with the time period and other requirements specified in the agreement, law, court order or arbitration award.
 - (5) An employer may not require or permit an employee to—
 - (a) repay any remuneration except for overpayments previously made by the employer resulting from an error in calculating the employee's remuneration; or
 - (b) acknowledge receipt of an amount greater than the remuneration actually received.

¹⁴⁵¹ Former CEO.

¹⁴⁵² Former CFO.

¹⁴⁵³ Crotty 2019:3.

¹⁴⁵⁴ Lex Mpati commission of enquiry 2018:7.

¹⁴⁵⁵ Public investment corporation

¹⁴⁵⁶ <https://www.businesslive.co.za/bd/national/2020-03-11-treasury-orders-pic-to-withhold-bonuses-from-its-executives> Accessed 11/3/2020.

fiduciary duties as an executive when he repeatedly concluded deals with individuals and entities even where no value had been proven from the first deals.¹⁴⁵⁷ The judicial commission further found that Matjila had a close relationship with businessman Iqbal Survé who was linked to AYO Technical Solutions when he supervised the R4.3 billion investment in AYO Technical Solutions. This close relationship "put down" pressure on the PIC team to approve investments. The PIC bought AYO shares at R43 each in 2017, which has since fallen to R2,30-meaning that R4 billion has evaporated from the value of the PIC's investment in the JSE.¹⁴⁵⁸ The commission's "dishonest" finding may result in Matjila being barred by the FSCA,¹⁴⁵⁹ a financial markets regulator, as a financial services and asset management professional. According to Sizwe Dlamini, in November 2020, Matjila applied for a review of the findings in the PIC Commission of Inquiry report.¹⁴⁶⁰

The commission concluded that there had been considerable impropriety at the PIC. The corporate governance processes were poor and ineffective, and the role and duties of the board and its sub-committees were unclear. There was a total disregard for due processes, and the victimization of employees was reported.¹⁴⁶¹

The commission identified that the current governance policies that were in place were inadequate, were not adhered to, and manipulated or intentionally circumvented to accomplish certain outcomes.¹⁴⁶² The board was found to be not functional, divided and conflicted. Non-executives failed in their oversight function during decision-making as their independence was questionable as they were also serving on the boards of investee companies.¹⁴⁶³ The board essentially "rubber-stamped" the decisions of the CEO without the necessary diligence to ensure that conditions were adhered to. Repeat investments were made to small companies (Lancaster/Steinhoff transactions), which indicates poor

¹⁴⁵⁷ <https://www.dailymaverick.co.za/article/2020-11-15-dan-matjila-fights-back-against-pic/> Accessed 12/5/2021.

¹⁴⁵⁸ <https://www.dailymaverick.co.za/article/2020-11-15-dan-matjila-fights-back-against-pic/> Accessed 13/5/2021.p2

¹⁴⁵⁹ Financial Sector Conduct Authority

¹⁴⁶⁰ <https://www.iol.co.za/business-report/companies/ex-pic-chief-dan-matjila-faced-with-unmerited-scrutiny> Accessed 13/5/2021.p1.

¹⁴⁶¹ Lex Mpati commission of enquiry 2018:778.

¹⁴⁶² Lex Mpati commission of enquiry 2018:778.

¹⁴⁶³ Lex Mpati commission of enquiry 2018:779.

risk management and non-adherence to the PIC' broad-based black economic empowerment policy.¹⁴⁶⁴

The commission found that IT systems used to ensure that all unlisted investments were automated were ineffective as certain transactions were managed by a manual system using spreadsheets. This created a risk of manipulation of records. The commission found that the CEO abused his powers and exerted undue influence over investee companies.¹⁴⁶⁵

6.2 LEX MPATI COMMISSION RECOMMENDATIONS

The commission recommended a review of the existing policies and the implementation of a comprehensive policy framework. Legislation, standard operating procedures and mandates were repeatedly violated. Executives failed to conduct themselves in a "fit and proper" manner and to act with integrity, honesty and in the best interest of their clients.

The process of appointing the board should reside with the PIC and director's affairs committee.¹⁴⁶⁶ Trade unions and depositors (such as government employees' pension funds) should not form part of the board. The PIC, not National Treasury, should source new directors; thereafter, the board must elect its chairperson rather than the Minister of Finance appointing the chairperson. Board members must be appointed based on skill and experience, not through a public process. The Minister of Finance and cabinet must approve the appointment of the elected board members. Board members should have a limited three years term of office, and the board members' main source of income should not be derived from PIC board fees. The reasons for removing a board member should be made public immediately. Regarding the structure of the PIC, the commission recommended that it be divided into three main specialist investment units. Decision-making on investments must be decentralised and done by the business units.¹⁴⁶⁷

¹⁴⁶⁴ Lex Mpati commission of enquiry 2018:780.

¹⁴⁶⁵ Lex Mpati commission of enquiry 2018:781.

¹⁴⁶⁶ Lex Mpati commission of enquiry 2018:779.

¹⁴⁶⁷ <https://www.businesslive.co.za/bd/national/2020-03-15-judicial-commission-recommends-vast-changes-to-governance-at-pic> Accessed 16/4/2020.

Policies and procedures should be reviewed regularly, and employees must familiarize themselves with all policies. The culture of the organization had to be improved, and the values of integrity, transparency and trust were instilled.

6.3 ZONDO JUDICIAL COMMISSION OF INQUIRY

The report on the judicial commission of inquiry into state capture was released in June 2022, wherein it was recommended that the duties and responsibilities of accounting officers are amended, and a provision was inserted which reads:

"[that] no person is criminally or civilly liable for anything done in good faith in the exercise or performance or purported exercise or performance of any power or duty in terms of the Prevention and Combatting of Corrupt Activities Act¹⁴⁶⁸ unless such person acts negligently."¹⁴⁶⁹

6.4 SUGGESTED COMMISSION

I am of the opinion that a commission similar to the New York State Commission on Public Authority Reform¹⁴⁷⁰ must be established in South Africa with the task of evaluating current corporate governance principles and practices and developing a strategy for improving standards of corporate governance, and recommending policies governing compliance, responsible oversight, and transparency. Key role players such as the DTI should issue guidelines on these points after consulting with the relevant stakeholders, establish structures, and develop processes and systems required to minimize the risk and prevent poor corporate governance. The commission must establish and maintain a culture of integrity through training and enforcing fiduciary duties. It is essential for the commission to establish and maintain a culture of integrity through training and the enforcement of fiduciary duties.¹⁴⁷¹ The duty of skill and care of directors should be formulated objectively to demand the skill and care reasonably expected of a person. It should be based on functions undertaken and not qualifications possessed.

¹⁴⁶⁸ Prevention and Combatting of Corrupt Activities Act 12 of 2004.

¹⁴⁶⁹ Judicial commission of inquiry report part 4 2022:25.

¹⁴⁷⁰ Millstein 2017:163.

¹⁴⁷¹ McGregor 2011:409.

7. REGULATORY BODIES

7.1 INDEPENDENT REGULATORY BOARD FOR AUDITORS (IRBA)

The IRBA is the independent auditing profession regulator mandated to protect the public and regulate audits performed by registered auditors. It differs from the SAICA,¹⁴⁷² which represents the interests of accountants. The IRBA acts as a custodian of the profession and develops internationally comparable standards and ethics to promote investment. The Steinhoff scandal and other high-profile scandals led to mandatory audit firm rotation from 2023 and the revision of the IRBA code of ethics.¹⁴⁷³ The fragmented regulation of different regulators makes it difficult to monitor systemic risk. IRBA proposes that comprehensive regulation of the auditing and accounting profession be done by the IRBA instead of creating a separate regulator of accountants.¹⁴⁷⁴

7.2 REGULATION

During periods of financial collapse and due to national interest, the state's intervention in critical aspects of corporate governance is justified. Several methods of state intervention are available, firstly to create a control block wherein the state appoints the board of directors and regulates the personal composition of the board. Secondly, the legislature enshrines certain strategic goals in the law for board members to adhere to and thereby steer policy directions and give effect to the state's goals.¹⁴⁷⁵

For the past two decades, the corporate governance form that the governance industry promoted was the best practices variety, also characterized as a "tick-box" exercise.¹⁴⁷⁶ In the case of Steinhoff, corporate governance evaluations measure only adherence to best practices and not integrity and business success. The corporate governance industry constantly modifies recommended best practices and creates new best practices; therefore, new avenues should be explored to regulate and enhance the quality of

¹⁴⁷² SA Institute of Chartered Accountants

¹⁴⁷³ <https://pmg.org.za/committee-meeting/29767/> Accessed 29/11/2020.

¹⁴⁷⁴ <https://pmg.org.za/committee-meeting/29767/> Accessed 29/11/2020.

¹⁴⁷⁵ Licht 2011:2.

¹⁴⁷⁶ Tingle 2018:232.

corporate governance.¹⁴⁷⁷ The key challenge is to resist a new or more detailed regulation process, which could result in resistance and reduce the sense of personal responsibility. Di Lorenzo's criticized the enforcement strategy in the United States, which focuses on large penalties to prevent misconduct and ignores the multiple cognitive influences on corporate behavior.¹⁴⁷⁸ A distinction must be made between problems that can be effectively addressed by new regulation and those that cannot be regulated by conventional means. To yield better results, unconventional governance processes must be explored, considering different world views, assumptions and myths for an effective paradigm shift from corporate governance being regulated through the law to corporate governance compliance through corporate governance codes based on comply and explained basis.¹⁴⁷⁹

8. CONCLUSION

As noted by Ronen, not all preventative measures are effective. Constructive legislative and regulatory intervention requires a sharp distinction between which causes can be reformed and which are resistant to legislative or regulatory intervention.¹⁴⁸⁰ Various screening guidelines, follow-up procedures, fraud models and red flag ratios are available to determine a company's financial standing. As Ojo stated, a company's core components are integrity and honesty.¹⁴⁸¹ I concur with Sharpe that corporate interactions between directors and CEOs determine whether effective monitoring is possible.¹⁴⁸² In the Steinhoff scenario, serious red flags were identified after applying the due diligence screening guidelines. Based on these red flags, management should have implemented investigative follow-up procedures, but that did not happen. The financial scandal could have been avoided if the due diligence guidelines and procedures had been applied. To strengthen their corporate governance role as gatekeepers and meet their fiduciary duties, board directors, auditors, and government regulators must be aware of the due diligence methodologies, board director benchmarking analysis, screening guidelines and follow-up

¹⁴⁷⁷ Tingle 2018:233.

¹⁴⁷⁸ Di Lorenzo 2017 207.

¹⁴⁷⁹ Winter 2011:3.

¹⁴⁸⁰ Ronen 2002:39.

¹⁴⁸¹ Ojo 2017:229.

¹⁴⁸² Sharpe 2012:5.

procedures. Investigative follow-ups should be made to improve corporate governance and prevent fraud and financial losses.

The collapse of Steinhoff is the result of failed corporate governance mechanisms. It significantly impacted various shareholders and stakeholders, including employees, pension funds, suppliers and customers. Financial markets and shareholders suffered substantial financial losses when share prices plummeted by more than 95% within the first week after Jooste resigned. Investors lost confidence in the accounting and auditing processes of Steinhoff. Worldwide, Steinhoff employees suffered job losses, and the company's collapse severely impacted their livelihoods. Others had their pensions and retirement savings tied up in Steinhoff shares and lost a significant portion of their savings. Many Steinhoff investors lost a substantial amount of their savings. Suppliers were negatively impacted by the collapse of Steinhoff and had to write off debts which impacted their profitability and cash flow. Overall, the collapse of Steinhoff had a significant impact on a wide range of stakeholders, and its effects are likely to be felt for many years to come.

CHAPTER 8: CONCLUSION

1. INTRODUCTION

This chapter concludes the research with a summary, findings and recommendations.

2. SUMMARY

I agree with academics that corporate governance has no precise definition.¹⁴⁸³ The internal management and control of the company is typically referred to as the company's corporate governance. Most definitions centre on internal governance within the corporation as opposed to oversight from the shareholders and stakeholders. Corporate collapse demonstrates an inherent absence and lack of effective corporate governance principles and practices and failure to ensure greater accountability by senior management.

Regardless of the outcome of any legal proceedings, the Steinhoff saga emphasizes the importance of management overseeing the implementation of key governance performance areas and effective stakeholder involvement and shareholder activism in decision-making.

3. RE-VISITING THE RESEARCH THESIS

The Steinhoff scandal has led to heightened scrutiny of corporate governance practices and a renewed emphasis on the significance of accountability and transparency in corporate decision-making. The fiduciary duties in corporate governance and the potential repercussions when directors and officers fail to fulfil their fiduciary obligations need to be emphasized.

4. OBSERVATIONS

¹⁴⁸³ Bloomfield 2013:10. Shleifer and Vishny 1997:734.

Historically, financial crises and corporate collapse have been driven by excessive risk-taking, deception, lack of ethics and greed.¹⁴⁸⁴ Over time, the approach to corporate governance has evolved to reflect the level of perceived risk at any given point in time. Following each financial crisis, the government promulgates many new laws to strengthen reporting requirements and controls, resulting in more robust corporate laws. As prosperity ensues, companies challenge growth-limiting restrictions, and the cycle continues.

5. RECOMMENDATIONS

Corporate governance is fluid and subject to change, as evidenced by various corporate failures worldwide, necessitating modifications to national and international law. The economy, economic competitiveness, well-being, and social well-being of South Africa are all directly impacted by good governance.¹⁴⁸⁵ The Steinhoff saga demonstrates no company can afford to turn a blind eye to unethical business practices and accounting irregularities.¹⁴⁸⁶ Good corporate governance and corporate citizenship should begin with corporate legal practitioners and auditors assisting boards and managers in decision-making to ensure compliance with the applicable law and increased internal monitoring of corporate governance practices.¹⁴⁸⁷

The goal of corporate governance is not solely to align the interests of directors and shareholders. It is to focus on the long-term economic health and value of the corporation as a whole.¹⁴⁸⁸ This viewpoint emphasizes codetermination which is a theory based on the notion that all the investors of the corporation should form part of the governance of the corporation. Employees are investors in a corporation. They invest their specific skills related to the corporation and time in the long-term interest of the corporation and also need to be actively involved in the governance of the corporation.¹⁴⁸⁹

The government is responsible for developing multi-stakeholder corporate governance codes by adhering to international corporate governance norms and standards and establishing common frameworks across public and private sectors to prevent corporate

¹⁴⁸⁴ Alsharqawi and Alsharqawi 2019:70.

¹⁴⁸⁵ Mongalo 2004:95.

¹⁴⁸⁶ Wade 2002:107.

¹⁴⁸⁷ Wade 2002:107.

¹⁴⁸⁸ Crawford 2009:912.

¹⁴⁸⁹ Trimble 2019:174-175; Crawford 2009:906-908.

governance collapse.¹⁴⁹⁰ Attention should be given to the state's civil liability for its involvement in the corporate governance collapse. Trust, support from government and sharing of risks between government and corporation are essential components of the evolution of corporate governance.¹⁴⁹¹

Corporate civil liability for South African nationals involved in international corporate governance collapses should be emphasized.¹⁴⁹² Concerns have been raised by various stakeholders, shareholders and institutional investors that no effective criminal sanctions are in place to hold those directors who recklessly managed and contributed to the collapse of a corporation legally accountable.¹⁴⁹³

A fundamental review of the current corporate governance principles and systems are complex and strategic recommendations should be widely assessed in relation to the long-term interests and the impact it will have on stakeholder, shareholders, and international relations.¹⁴⁹⁴ I concur with the views of Wiese¹⁴⁹⁵ and Parry¹⁴⁹⁶ that increased or excessive corporate governance regulation will burden companies, reduce their ability to take risks, and inhibit growth and competitiveness, which is crucial for economic development.¹⁴⁹⁷

South Africa needs to develop a mixed framework of strong corporate governance mandatory rules and a set of non-mandatory rules¹⁴⁹⁸ that ensure effective remedies for transgressions and encourages transparency, integrity, and international competitiveness.¹⁴⁹⁹ In *Mthimunye-Bakoro v Petroleum Oil and Gas Corporation of South Africa*,¹⁵⁰⁰ the court confirmed the significance of corporate governance in improving efficiency, organisational performance, and resource allocation. The effectiveness of controls and safeguards imposed upon directors to make decisions in the company's best interest, including the business judgment rule and the court's general discretion to relieve

¹⁴⁹⁰ Hamann 2004:288.

¹⁴⁹¹ Rodrigues and Sangster 2012:18.

¹⁴⁹² Horrigan 2007:94.

¹⁴⁹³ Alsharqawi and Alsharqawi 2019:69.

¹⁴⁹⁴ Crawford 2009:910-913.

¹⁴⁹⁵ Wiese 2018:178.

¹⁴⁹⁶ Parry 2014:16.

¹⁴⁹⁷ Alsharqawi and Alsharqawi 2019:69.

¹⁴⁹⁸ Krackhardt 2005:332.

¹⁴⁹⁹ Mongalo 2004:97.

¹⁵⁰⁰ *Mthimunye-Bakoro v Petroleum and Gas Corporation of South Africa Limited* 2015 JOL 33744.

a director either wholly or partly from liability,¹⁵⁰¹ are influenced by various policy considerations and prevailing social responsibilities towards society.¹⁵⁰² Corporate risk management is becoming an essential part of directors' responsibilities, especially new risks such as cybercrime and digital crime that are on the increase.¹⁵⁰³

A fundamental review of the current corporate governance principles and systems are complex and strategic recommendations should be widely assessed in relation to the long-term interests and the impact it will have on stakeholder, shareholders, and international relations.¹⁵⁰⁴

6. QUESTIONS FOR FURTHER RESEARCH

I believe shareholder activism in the prevention of corporate governance failure is another domain promising much research and development in the manner corporations are governed.

Further research is necessary to re-evaluate the conventional processes and assumptions governing corporate governance. The framework for corporate governance must incorporate comprehensive policies and procedures that promote transparency, accountability, and ethical and responsible management conduct. Companies should develop management programs that include establishing a robust corporate governance framework, implementing internal controls, and developing a robust culture of integrity. I concur with Sharpe that further engagement with organisational behaviour theories is required to identify the attributes and selection criteria required to elect an independent and assertive board of directors who meaningfully evaluate and challenge management decisions and ensure the board's effective governance.¹⁵⁰⁸

¹⁵⁰¹ Section 77 (9) of the Act.

¹⁵⁰² Ramnath and Nmehielle 2013:101; Crawford 2009:913.

¹⁵⁰³ Calkoen 2020:8.

¹⁵⁰⁴ Crawford 2009:910-913.

¹⁵⁰⁵ Wiese 2018:178.

¹⁵⁰⁶ Parry 2014:16.

¹⁵⁰⁷ Alsharqawi and Alsharqawi 2019:69.

¹⁵⁰⁸ Sharpe 2011:1439.

7. CONCLUSION

The prevention of corporate failure remains, in my opinion, a complex endeavour. Legislation, codes of conduct, structures, and processes cannot resolve all problems on their own. The ethical and responsible behaviour of company directors, managers, and officers is crucial. Regardless of the outcome of any legal proceedings, the collapse of Steinhoff demonstrates the crucial role of the board, directors, auditors, company secretary, shareholders, and other stakeholders in ensuring that a company complies with all applicable legislation and ethical and legal standards and operates with integrity and transparency. Similar to Enron, I believe Steinhoff will become the new benchmark for measuring corporate governance failures.

I want to finally quote Arthur Levett (a former chairperson of the American Securities and Exchange Commission), who said:

"If a country does not have a reputation for strong corporate governance practices, capital will flow elsewhere. If investors are not confident with the level of disclosure, capital will flow elsewhere. If a country opts for lax accounting and reporting standards, capital will flow elsewhere. All enterprises in that country-regardless of how steadfast a particular company's practices may be-suffer consequences."¹⁵⁰⁹

And also Cicero¹⁵¹⁰ and Warren¹⁵¹¹ said:

"The good of the people is the greatest law."

"in civilized life, law floats in a sea of ethics."

¹⁵⁰⁹ Loubser 2002:140.

¹⁵¹⁰ Marcus Tullius Cicero Roman orator and philosopher (106-43 B.C.) <https://www.britannica.com/biography/Cicero> Accessed 06/02/2023.

¹⁵¹¹ The Honourable Earl Warren quoted in Fox 2002:867.

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