THE DUTY OF CARE AND SKILL, AND RECKLESS TRADING: REMEDIES IN FLUX?

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I INTRODUCTION

In terms of South African common law, directors of companies have two duties. First is fiduciary duties, which do not require fault for liability (a form of strict liability). Second is the duty of care and skill, which has always been accepted as delictual in nature.

The rationale behind the duty of care and skill is to prevent those in charge of the management of the company from allowing it to act in a manner that could harm such a company. The law therefore utilises the law of delict to hold these company stewards to account, and to make good the harm suffered by the wronged party, being the company which such wrongdoers are managing. The Companies Act[1] ('the Act') has to an extent codified the common law duty of care and skill of directors, and has confirmed that the liability for the breach of this duty is delictual in nature.

South African company law further provides that a company's business may not be conducted with gross negligence, 'recklessly' or fraudulently. In s 424 of the Companies Act 61 of 1973 ('the 1973 Act'), any person could hold another person liable who essentially allowed the company to conduct business in a reckless manner.[2] At face value, it appeared (and case law seems to have confirmed this) that the statutory remedy was intended primarily for creditors, and mostly utilised by such creditors when a company was in liquidation. Section 424 of the 1973 Act has been replaced by s 22(1), as read with section 77(3)*(b)* of the Act.

The Act, however, also provides that Chapter XIV of the 1973 Act continues to apply in respect of the liquidation of insolvent companies.[3]

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[1] Companies Act 71 of 2008.
[2] Section 424 of the 1973 Act.
[3] Schedule 5, item 9.

Section 424 of the Act is therefore in theory still available to creditors as long as a company is formally in liquidation.

The purpose of this article is to critically evaluate both forms of liability, and to determine their relationship, interaction and continued relevance. On the one hand, the article will attempt to show that the remedy in respect of breach of the duty of care and skill traditionally existed for the benefit of the company, a position which the Act confirms in section 77(2)*(b)*, but attenuates through the operation of business judgment rule. On the other hand, it will attempt to show that whilst the reckless trading provisions (with the consequent liability) was traditionally utilised by creditors, the current Act has seemingly deprived creditors of this remedy to some extent,[4] and that the company itself now has both remedies available to it.

Thus the issue becomes whether a company is in need of both, especially as liability based on reckless trading seems a less onerous remedy from a litigant-company's perspective. Why would a company pursue a remedial avenue (breach of the duty of care and skill) if such a course of action is more burdensome than an alternative remedy of similar effect?

Within this critical assessment of the two remedies, the article will further argue that the remedial dispensation of creditors has also undergone a significant change, and that the current remedy for reckless trading has supplanted the creditors with the company as the primary claimant. It will further show why this, counter-intuitively, is an appropriate change. The focus will be on insolvent companies, before and after formal liquidation.

II THE DUTY OF CARE AND SKILL

(a) Common law

The duty of care and skill is delictual in nature and any liability of a director for damages which he causes the company is based on delictual principles,[5] yet the inquiry around care and skill centres primarily on negligence.[6] It is a received product of English tort law, as modified to function within the South African abstract and largely Roman-Dutch

[4] Section 218 of the Act will be considered below.

[5] Bouwman, 'An appraisal of the modification of the director's duty of care and skill' (2009) 21 *SA Merc LJ* 509 at 510, and Kennedy-Good & Coetzee, 'The business judgment rule (Part 2)' (2006) *Obiter* 277 at 281.

[6] Cassim (ed) et al, *Contemporary Company Law* 2 ed (Juta 2012) 554.

chassis of delict.[7] The exact legal position relating to the common law standard has remained unclear,[8] and it must be noted from the outset that the remedy's successful use is an exceptionally rare occurrence.[9]

In the English decision of *In re Brazilian Rubber Plantations and Estates Limited*[10] ('*Brazilian Rubber*'), widely regarded as the founding case for the modern duty of care and skill, the court (Chancery Division) held that a director should act with the degree of care as could be reasonably expected of him, taking into consideration his knowledge and experience.[11] The court further held that such a director is not expected 'to bring any special qualifications to his office'.[12] Reasonable care for the court meant the care which an ordinary person would be expected to take in the same circumstances, and mere errors of judgment could not be a basis for liability.[13]

Re City Equitable Fire Insurance Co Ltd ('*Equitable Fire*') adds to this by making two points. The first is that '[i]n ascertaining the duties of a director of a company, it is necessary to consider the nature of the company's business and the manner in which the work of the company is, reasonably in the circumstances and consistently with the articles of association, distributed ...'. Second is that the duty requires only that a director display: honesty; the type of care to be expected from an 'ordinary man', but not 'a greater degree of skill than may reasonably be expected from a person of his knowledge and experience'; and need not give the business' affairs constant attention (as his duties are of an 'intermittent nature').[14]

What is clear from the early English pronouncements is that, if a director acted honestly,[15] an error of judgment was not regarded as actionable unless there was gross negligence.[16] Over time, the duty thus formulated, alongside many other fundamental principles of English company law, found reception in South African jurisprudence.

[7] The dynamics of its interaction with *King II* and *King III* are beyond the scope of this article.

[8] Bekink, 'An historical overview of the director's duty of care and skill: From the nineteenth century to the Companies Bill of 2007' (2008) 20 *SA Merc LJ* 95 at 95.

[9] Jones, 'Directors' duties: negligence and the business judgment rule' (2007) 19 *SA Merc LJ* 326 at 326–327 and 332. See also Bouwman, (2009) 21 *SA Merc LJ* 509 at 526, stating that there is only one reported successful case — *Niagara Ltd (in liquidation) v Langerman & others* 1913 WLD 188.

[10] *In Re Brazilian Rubber Plantations And Estates Limited* [1911] Ch 425.

[11] *In Re Brazilian Rubber* para 430.

[12] *In Re Brazilian Rubber* para 430.

[13] *In Re Brazilian Rubber* para 430.

[14] *Re City Equitable Fire Insurance Co Ltd* [1925] Ch 407.

[15] Bekink, (2008) 20 *SA Merc LJ* 95 at 98.

[16] Bekink, (2008) 20 *SA Merc LJ* 95 at 97.

However, these cases remained highly influential. The leading South African case on the duty of care and skill of directors is *Fisheries Development Corporation of SA Ltd v Jorgensen,*[17] where the court makes a number of seminal observations.

First and foremost is the delictual element of negligence, which under this remedy is somewhat modified. First, the nature of the company's business as well as the duties of a director are determinative of the extent of the duty of care and skill required of a director.[18] Second, directors' duties and qualifications are not analogous to those of an auditor or an accountant,[19] and neither special business expertise, nor intimate knowledge of the business is required.[20] What is expected of a director is simply that he exercises 'the care which can reasonably be expected of a person with *his* knowledge and experience'.[21] Whilst such a director may receive, accept and rely on the advice of others, ultimately he must exercise his own judgment.[22]

From the above, as well as academic commentary, it is generally accepted that, despite the primacy of delictual negligence in the inquiry, the common law duty of care and skill is at heart more subjective than objective — the individual director is considered, and is neither measured against the reasonable person nor against the reasonable director, but what the reasonable thing would have been for *such a director* to have done.[23]

Thus, on the other hand, there is also an objective dimension to the standard, i e that 'reasonable' care can be established objectively. Broadly speaking, it could be stated that the 'reasonable' element is objective, yet the 'man' element is subjective.[24] Whether fundamentally subjective or

[17] *Fisheries Development Corporation of SA Ltd v Jorgensen; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd* 1980 (4) SA 156 (W).

[18] *Fisheries Development Corporation of SA Ltd* para 165 — such that non-executive directors, unlike executive directors, are not required to pay continuous attention to the business of the company because their duties are intermittent in nature, performed at board meetings as and when they are held. Non-executive directors are, however, not bound to attend these board meetings.

[19] *Fisheries Development Corporation of SA Ltd* para 165.

[20] *Fisheries Development Corporation of SA Ltd* para 165.

[21] *Fisheries Development Corporation of SA Ltd* para 165 [own emphasis].

[22] *Fisheries Development Corporation of SA Ltd* para 165, and generally for the above Bekink, (2008) 20 *SA Merc LJ* 95 at 100–101, Bouwman, (2009) 21 *SA Merc LJ* 509 at 510–511 and 514–515.

[23] Cassim (ed) et al, (Juta 2012) 558; Cassidy, 'Models for reform: The directors' duty of care in a modern commercial world' (2009) 20(3) *Stell LR* 373 at 376 & 383–385; see also the commentary of Bekink, (2008) 20 *SA Merc LJ* 95 at 99–103 as well as Bouwman, (2009) *SA Merc LJ* 509 at 510–512.

[24] It has also been stated that 'care' is the objective and 'skill' the subjective elements respectively — Bouwman, (2009) 21 *SA Merc LJ* 509 at 510.

objective,[25] it is clear that one is dealing at least with a practically *differentiated* 'reasonable director', rooted in the facts of each case as it is considered. It has also been argued, correctly, that the 'subjective' element is as much a function of its mixed legal heritage as it is a function of the variable nature of directorship itself.[26]

(b) Statutory law: potential divergence and the effect of the business judgment rule

The Act codifies the duty of care and skill without abolishing the common law.[27] Yet the codification may have brought about a divergence between the common law and statutory tests for care and skill respectively. There are, in essence, two competing views, of which a brief analysis is made below.

The position in favour of a broadly non-disparate common law and statutory duty is succinctly stated by Du Plessis.[28] Here it is argued that the statutory test for the reasonable director remains subjective, as the objective dimension of the 'reasonable director' is attenuated by a pre-emptive and *subjective* 'setting' of the standard with reference to the knowledge and skill of the particular director in question, potentially upwards but generally downwards. This approach follows *Fisheries Development Corporation of SA Ltd v Jorgensen* as discussed above.[29]

Yet as noted, South African courts have largely been influenced by English precedents in the interpretation of the duties of directors.[30] Starting from *Dorchester Finance Co Ltd v Stebbing*,[31] the English courts have begun to interpret their counter-equivalent statutory formulation of the duty in an increasingly objective manner, allowing an upward adjustment for more knowledgeable directors, but no downwards adjustment below the standard set by the 'ordinary' reasonable person.[32] Lord Justice Hoffman in particular has lead the charge, basing his

[25] It is not within the scope of this article to consider this debate in any detail.

[26] This is as the subject of the duty is not, as ordinarily in delict, a legal person, but rather the legal *capacity* in which a person is acting — see, for example, Bekink, (2008) 20 *SA Merc LJ* 95 at 102; and also Cassidy, (2009) 20 *Stell LR* 373 at 385.

[27] Section 76(3)*(c)*.

[28] Du Plessis, 'Directors' duty of care skill and diligence' in Mongalo (ed) *Modern Company Law for a Competitive South African Economy* (Juta 2010) 263.

[29] See s 2*(a)* supra, and n17.

[30] Bekink, (2008) 20 *SA Merc LJ* 95 at 102.

[31] [1989] BCLC 498.

[32] See Bekink, (2008) 20 *SA Merc LJ* 95 at 99.

approach on the formulation found in s 214(4) of the Insolvency Act of 1986, and effected a broad change on the approach of English common law.[33]

What makes this second, more objective and stricter approach significant is the wording of the current Act. The partial codification of the duty of care and skill, introduced in s 76(3)*(c)* of the South African Companies Act, appears to be lifted largely[34] from the wording of the new United Kingdom Companies Act, which adopted, by and large, the same wording as the Insolvency Act mentioned above. Therefore, it is quite possible that a more objective, upwardly adjustable formulation of the duty, as in the English judgments cited,[35] is the true manner in which to approach this provision.[36]

The common law position remains aligned to the *Jorgensen* case, but it is thus arguable that the scope of the statutory duty is narrower, and only adjustable upwards beyond the ordinary standard of the diligens paterfamilias.[37] The strictest interpretation would be that the test, supported by the appearance of some objective measures within the wording of the statutory provision, has been brought closer to the original principles of delict, and that the standard of care is objective and adjustable only upwards. The subjective differentiation becomes a secondary question based on the factual matrix at hand.[38]

For a detailed discussion of this topic in particular, however, see the contributions of Du Plessis,[39] and Cilliers et al,[40] and Cassidy,[41] Bekink,[42] and Bouwman,[43] alongside the English cases and other authority cited. The strictest interpretation possible places the highest burden on the analysis below, and thus is the most careful and

[33] See Bekink, (2008) 20 *SA Merc LJ* 95 at 99; Bouwman, (2009) 21 *SA Merc LJ* 509 at 512. See also the judgments found in *Norman v Theodore Goddard* [1991] BCLC 1028 (CLD); *Re D'Jan of London Ltd* [1994] 1 BCLC 561 (Ch); *Cohen v Selby* [2001] 1 BCLC 176, CA paras 10 and 21; *Re Westlowe Storage and Distribution Ltd* [2000] 2 BCLC 590, 611, to name a few.

[34] With the exception of the addition of 'diligence' — a seemingly Australian contribution, as per Du Plessis, 'A comparative analysis of directors' duty of care, skill and diligence in South Africa and in Australia' (2010) *Acta Juridica* 263 at 268.

[35] Cf n33.

[36] This has also been argued to be the better approach — Cassidy, (2009) *Stell LR* 373 at 375 & 377.

[37] Cassidy, (2009) 20 *Stell LR* 373 at 377 & 385–386.

[38] Bekink, (2008) 20 *SA Merc LJ* 95 at 111, Bouwman, (2009) 21 *SA Merc LJ* 509 at 513–514, and n37 above.

[39] Du Plessis, (2010) *Acta Juridica* 263 at 263.

[40] Cilliers et al, *Cilliers and Benade: Corporate Law* 3 ed (Butterworth 2000) 147 paras 10.30–10.32.

[41] Cassidy, (2009) 20 *Stell LR* 373 at 376 & 383–385.

[42] Bekink, (2008) 20 *SA Merc LJ* 95 at 8.

[43] Bouwman, (2009) 21 *SA Merc LJ* 509.

appropriate approach, and will be used when discussing the impact of the business judgment rule.

(i) The impact of the business judgment rule

The test for breach of the statutory duty of care and skill (as well as some of the statutory directors' fiduciary duties) in the current Act's regime is attenuated by another new element. This is the so-called 'business judgment rule', found in s 76(4)*(a)* of the Act. It has a profound impact on the standard of conduct inherent in the statutory duty of care and skill.

The Act, shortly, stipulates in s 76 that:

> '(4) In respect of any particular matter arising in the exercise of the powers or the performance of the functions of director, a particular director of a company-
> *(a)* will have satisfied the obligations of subsection (3)(b) and (c) if ...'.

the director has 'made a decision, or supported 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'.[44]

There are other components to this rule (for instance relating to the use of information or reliance on the performance of others), but the focus here is on the effect of the above excerpt of the section. At the core of this rule is the establishment of a rebuttable presumption that a director has acted (1) in good faith, (2) on an informed basis, and (3) with the honest belief that the best interests of the company will be served.[45] That is the essence of the standard of review found in the business judgment rule.[46]

Whilst it is still far from settled who bears the onus of proof regarding s 76(4),[47] a company would only be successful if it cannot be proven that: (1) a director took 'reasonably diligent steps to become informed about the matter',[48] *and* (2) had no 'material personal financial interest in the subject matter of the transaction',[49] *and* (3) factually 'took a

[44] Section 76(4)*(a)*(iii) [own emphasis].

[45] Bouwman, (2009) 21 *SA Merc LJ* 509 at 523, Jones, (2007) 19 *SA Merc LJ* 326 at 329, Cassidy, (2009) *Stell LR* 373 at 398, and Kennedy-Good & Coetzee, 'The business judgment rule (Part 1)' (2006) *Obiter* 62 at 65 & 70.

[46] See Kennedy-Good & Coetzee, (2006) *Obiter* 62 at 63 & n12.

[47] Cassim (ed) et al, (Juta 2012) 565.

[48] Section 76(4)*(a)*(i).

[49] Section 76(4)*(a)*(ii).

decision', *and* (4) 'had a rational basis for believing that the decision was in the best interests of the company', *and* (5) 'did [indeed] believe ... the decision was in the best interests of the company'.[50] In s 76(4)*(b)* read with s 76(5), the director is 'entitled to rely on' (i e read: *not liable if he did rely on* ...) the performance of certain persons and certain information.

Therefore — in the absence of personal interests and the exculpatory effect of s 76(5) — the two salient requirements arising from the business judgment rule would seem to be the taking of reasonable steps to ensure a decision is informed, as well as the two-step requirement of believing a decision to be in the best interests of the company and having a rational basis for that belief.

As a starting point, a director might act to ensure that he has no undisclosed personal interests and take reasonably diligent steps to inform himself of material considerations and facts when taking a decision, but these are merely *steps* he may follow to ensure he complies with s 76(3)*(c)* via s 76(4). It is quite clear, however, that the underlying consideration of compliance with the duty of care and skill, as far as the business judgment rule is concerned, remains the rational-basis requirement found in s 76(4)*(a)(*iii).[51]

It is crucial not to conflate the concepts of reasonableness and rationality. In the context of fiduciary duties (specifically the proper exercise of powers by directors) Rogers J, in *Visser Sitrus (Pty) Ltd v Goede Hoop Sitrus (Pty) Ltd and others*,[52] gives a measure of content to the 'rationality requirement' of this rule. The dictum begins by stating:[53]

> 'Section 76(4) makes clear that the duty imposed by s 76(3)*(b)* to act in the best interests of the company is not an objective one, in the sense of entitling a court, if a board decision is challenged, to determine what is objectively speaking in the best interests of the company. What is required is that the directors, having taken reasonably diligent steps to become informed, should subjectively have believed that their decision was in the best interests of the company and this belief must have had "a rational basis". The subjective test accords with the conventional approach to directors' duties ...'.

[50] Section 76(4)*(a)*(iii).

[51] Cassidy, (2009) 20 *Stell LR* 373 at 375; in contrast to cl 91(2) of the Companies Bill of 2007, which required 'reasonableness' — Bouwman, (2009) 21 *SA Merc LJ* 509 at 528; Jones, (2007) 19 *SA Merc LJ* 326 at 329–330.

[52] 2014 (5) SA 179 (WCC).

[53] *Visser Sitrus (Pty) Ltd* para 74.

The court then further states that:[54]

> 'Section 76 requires the *bona fide* assessment of the directors to have a rational underpinning. This requirement has been articulated less frequently in the conventional statement of directors' duties, but is not necessarily an innovation.'

However, the analysis of a decision's rational basis is objective in nature, whilst the quality of the decision introduces certain subjective elements relating to the director in question.[55] It is here that the court engages in a creative exercise of judicial cross-pollination, and turns to the readily comparable principles of administrative law for clarity. Specifically, it looks to jurisprudence regarding the 'rationality' criterion available as a ground for review of administrative action as per s 6(2)*(f)*(ii) of the Promotion of Administrative Justice Act, (herewith referred to as 'PAJA')[56] and more generally (and to the point) the legality principle in this field in general.[57]

Subsections *(aa)*–*(dd)* of s 6(2)*(f)*(ii) of PAJA point to, respectively, the purpose of the administrative action, the purpose of its authorising provision, the information available to the administrator, and the reasons provided, as benchmarks to which the action must bear a 'rational connection'. This section from PAJA further underscores the more general meaning attributed by the court to rationality, as hinging on the relationship between the power being exercised, and the purpose for which it was conferred. To quote, the question then becomes '... [w]as the decision or the means employed rationally related to the purpose for which the power was given?'[58]

What this means for s 76(4)*(a)*(iii) of the Act is that, as it does in the context of legality,[59] is that the courts' role is not to supplant the judgment of an actor in matters of how he should have exercised the corporate powers conferred. Moreover, the inquiry is limited, and any consideration of the 'merits and the wisdom of business decisions' is

[54] *Visser Sitrus (Pty) Ltd* para 75.

[55] *Visser Sitrus (Pty) Ltd* para 76 — cf. below at s 2*(b)*(ii), and n49 above. See also Jones, (2007) 19 *SA Merc LJ* 326 at 332; Cassidy, (2009) 20 *Stell LR* 373 at 398–399.

[56] of 2000 ('PAJA').

[57] *Visser Sitrus (Pty) Ltd* para 74.

[58] *Visser Sitrus (Pty) Ltd* para 75, and the authorities quoted therein: *Association of Regional Magistrates of Southern Africa v President of the Republic of South Africa & others* 2013 (7) BCLR 762 (CC) paras 49–50, and *Minister of Defence and Military Veterans v Motau & others* [2014] ZACC 18 para 69.

[59] *Visser Sitrus (Pty) Ltd* para 74 — see *Pharmaceutical Manufacturers Association of SA & another: In re Ex Parte President of the Republic of South Africa & others* 2000 (2) SA 674 (CC) as per Chaskalson P (as he then was) para 90; see also *Carephone (Pty) Ltd v Marcus NO & others* 1999 (3) SA 304 (LAC) para 36.

quite strictly beyond the ambit of the courts' purview.[60] It is rather to determine whether the decision factually made, was rationally related to the purpose for which that power to make such a decision was conferred. In other words, the court applies this construction of the rationality of the exercise of a public power ('with modifications') to the exercise of a corporate power by a corporate actor.[61]

The final question is then whether this construction — appearing in the context of fiduciary duties — can be applied to the duty of care and skill in s 76(3)*(c)*. It has been widely stated that the business judgment rule relates to the duty of care and skill on the basis of 'decision-making'.[62] The statutory approach to this duty remains a question of whether a director *subjectively* exercised his powers and performed his functions in a *manner* (i e a qualitative approach in keeping with the duty of care and skill's focus on 'how', compared to the 'what' of fiduciary duties) that is consistent with the way in which an *objectively* reasonable director with the company's best interests at heart would have done.

Yet in the current companies regime, there is a pre-emptive 'gatekeeper' in the form of the criterion of rationality — an imperative of s 76(4)*(a)*(iii) of the Act. In cases where s 76(3)*(c)* is involved, the rational relationship must exist between (1) the belief and concomitant decision (the 'assessment' as per Rogers J, above), and (2) the reasoning behind it (the 'underpinning' as per Rogers J, above). This innovative approach, borrowing from pre-existing legal doctrine on rationality, may not necessarily stand the test of time, but provides a useful starting point as far as case law authority on s 76(4) is concerned.

Thus the law currently seems to require that, objectively speaking and without regards to the merits of the decision,[63] there is no rational connection whatsoever between (1) a belief on the part of a director that a specific exercise of his powers would be in the best interests of the company, which belief results in a concrete decision or judgment, and (2) the reason for the director holding such a belief, and acting

[60] Cassim (ed) et al, (Juta 2012) 565, Bouwman, (2009) 21 *SA Merc LJ* 509 at 525 & 531, and Kennedy-Good & Coetzee, (2006) *Obiter* 62 at 70–71. See also *Levin v Felt & Tweeds Ltd* 1951 (2) SA 401 (A) para 414 to the effect that:

> '[i]n the absence of any allegation that the directors acted *mala fide* this amounts to asking this Court to usurp the functions of the directors and to consider what is the best for the company from the business point of view. This is not the function of a Court of law.'

[61] *Visser Sitrus (Pty) Ltd* para 78.

[62] Jones, (2007) 19 *SA Merc LJ* 326 at 329, and Kennedy-Good & Coetzee, (2006) *Obiter* 62 at 64.

[63] And in all likelihood also to some degree dependent on the circumstances — Jones, (2007) 19 *SA Merc LJ* 326 at 330.

thereupon. It is submitted that this is a far more forgiving threshold than the standard of reasonableness found in the care and skill inquiry.

Whether *procedurally* it functions as a defence to the care and skill inquiry, functions to negate the cause of action for such a claim, or is part and parcel of the inquiry itself,[64] the business judgment rule has an important effect on s 76(3)*(c)*. If s 76(4) is to function in certain cases as a shield against liability for the breach of the duty of care and skill, it logically cannot set a higher or equivalent standard of conduct than the one prescribed by the duty of care and skill itself.

Following this reasoning, on the spectrum of conduct which exists between excessive reasonableness and the most severe gross negligence, there must be a portion that lies between (1) the most severe gross negligence, and (2) the most tenuously acceptable reasonableness, which *is not covered* by s 76(4) — otherwise s 76(3)*(c)* will be rendered redundant. Put simply: if a director acted unreasonably, he may yet escape liability because he acted at least rationally. The question is therefore: how unreasonably may a director act before he cannot be protected by the defence of a rational basis for his decision? The degree to which the business judgment rule's import of rationality encroaches on what would (but for its effect) have been considered a breach of the duty of care and skill is the focus of the next section.

(ii) The bottom line: gross negligence?

What is clear from Section II is that the common law test for negligence in (what could be termed 'ordinary') delictual actions has been adapted for the inquiry relating to the care and skill of directors. At common law, there is a subjective attenuation of that standard, lowering it to that of the reasonable director with the same knowledge and experience as the director is question. Nonetheless, assuming — to the detriment of any directors' legal position — that the *statutory* standard has become adjustable upwards only, what is the effect of rationality, and the business judgment rule in general on that standard?

In short, the portion of the spectrum that would 'activate' liability in care and skill cases is made smaller than the activating portion of the spectrum in ordinary delict. Directors can therefore — in a manner of speaking — act *more* unreasonably than other hypothetical actors in the sphere of delict.[65] The business judgment rule compounds this, further

[64] Elements of the section which are, again, not within the scope of this article, and better left to an in-depth analysis of their own.

[65] See also Jones, (2007) 19 *SA Merc LJ* 326 at 327.

narrowing the potential for liability and allowing even more unreasonable conduct to escape liability.

This is clear from *Visser Sitrus,* which states that:[66]

> '[The] rationality criterion as laid down in s 76 is an *objective* one, but its threshold is quite different from, and more easily met than, a determination as to whether the decision was objectively in the best interests of the company.'

By setting an exculpatory standard of rationality, which ostensibly excludes any judicial consideration of the merits of directors' decisions,[67] s 76(4) also substantially narrows the potential scope of liability in terms of s 76(3)*(c)*. Its effect is that an objectively *unreasonable* decision also cannot result in liability if it was (1) reasonably informed, and (2) rational in relation to its basis.

Comparatively, the jurisprudence of the United States (from which the business judgment rule originates, and where all directors' duties are combined, and subject to its effect)[68] indicates that the rule serves to cover all but the most serious cases of directors' ill-judgment,[69] and has limited the application of care and skill.[70] In the United States, rationality allows far more discretion than reasonableness. Conversely, the Australian version of the statutory business judgment rule provides that such a 'belief or judgment' about the best interests of the company 'is a rational one unless the belief is one that *no reasonable person* in [the directors'] position would hold.'[71] This seems to indicate, and it has been stated as such, that reasonableness is the benchmark for rationality in the Australian context.[72]

Yet neither of these positions could hold 'out and out' in South Africa. If reasonableness were the test for rationality, the scope of conduct permitted by s 76(4) would be lesser or identical to the scope of conduct permitted by the standard of care and skill, and logically the former would have little or no effect save to redundantly reinforce the ordinary standard for care and skill. On the other hand, it is generally accepted

[66] *Visser Sitrus (Pty) Ltd* para 76 [own emphasis].

[67] See n60 supra.

[68] Bouwman, (2009) 21 *SA Merc LJ* 509 at 531.

[69] Hansen, 'The ALI Corporate Governance Project: Of the duty of due care and the business judgment rule' (1986) 41 *Bus Law* 1257 — as in Cassim (ed) et al, (Juta 2012) 565 and n264.

[70] Jones, (2007) 19 *SA Merc LJ* 326 at 327.

[71] Austin & Ramsay, *Ford's Principles of Corporations Law* 14 ed (LexisNexis 2010) 437 [own emphasis].

[72] Idem at 440.

that the American version of the rule is constituted too widely for South African jurisprudential tastes.[73]

It is not the aim of this section to state categorically that rationality for the purposes of s 76 is pure rationality as fully differentiated from reasonableness — merely to opine that in light of the *Visser Sitrus* decision as well as a cold, objective reading of the relevant provision, the law seems to indicate a construction where the two concepts do not, contextually, have identical content; as well as a construction where rationality is a lower standard than the subjective standard of reasonableness for care and skill.

Commercial activity entails risk, and decision-making in business often involves the conscious and active taking of risks.[74] Indeed it is one of the fundamental jurisprudential policy pillars of the rule itself.[75] Nonetheless, under the current companies' regime, directors making such decisions are required to display a set standard of care and skill in the making of those decisions. Yet they are *deemed* to have acted with the necessary care and skill if their (informed) actions have a rational connection with the beliefs or value judgments that underlie them. This leads to the crucial question: is there any practical difference between negligent conduct that is so unreasonable that it cannot even be characterised as rational, and *gross* negligence?

Consider the meaning of gross negligence, which sits at the far end of the spectrum of conduct. As confirmed by *Philotex (Pty) Ltd and others v Snyman and others; Braitex (Pty) Ltd and others v Snyman and others,*[76] in *Portnet v The Owners of the MV 'Stella Tingas'*[77] Scott JA defines the concept as follows:[78]

> '... [T]o qualify as gross negligence the conduct in question, although falling short of *dolus eventualis*, must involve a departure from the standard of the reasonable person to such an extent that it may properly be

[73] The rule is 'radically different', comparatively speaking — Jones, (2007) 19 *SA Merc LJ* 326 at 327.

[74] See, for example, Bekink, (2008) 20 *SA Merc LJ* 95 at 98 and 113–114, Bouwman, (2009) 21 *SA Merc LJ* 509 at 523–524.

[75] Alongside the non-deterrence of competent persons in becoming directors, avoiding judicial supplanting of directors' decisions, preventing shareholders from usurping directors in matters of management, and keeping existing 'market mechanisms' fulfilling the same function unhindered — Bouwman, (2009) 21 *SA Merc LJ* 509 at 523–524 and Kennedy-Good & Coetzee, (2006) *Obiter* 62 at 65–66.

[76] 1998 (2) SA 138 (SCA), in the more commercial context of reckless trading — cf. for example, Cassim (ed) et al, (Juta 2012) 591 and generally for the above Bekink, (2008) 20 *SA Merc LJ* 95 at 101.

[77] *Transnet Ltd t/a Portnet v The Owners of the MV 'Stella Tingas' & another* [2003] 1 All SA 286 (SCA).

[78] *Transnet Ltd t/a Portnet* paras 290–291.

> categorized as extreme; it must demonstrate, where there is found to be conscious risk-taking, a complete obtuseness of mind or, where there is no conscious risk-taking, a total failure to take care. If something less were required, the distinction between ordinary and gross negligence would lose its validity.'

Thus, consider the position of a company-plaintiff. In order to get past the business judgment rule, the rational relationship between the belief and the resultant decision has to be assailed. In other words, without relying on the merits of the decision, it has to be shown that a director's decision to *take a specific risk* (ostensibly in the company's interests) was wholly without a rational basis. As such, the director's belief (or 'business judgment' as it were) underlying a decision must be shown to be entirely baseless.

This is by no means impossible, but it would imply that the risk-taking on the facts demonstrates attributes very close to a 'complete obtuseness of mind',[79] and was therefore extremely unreasonable. Reasonableness and rationality are both *standards of human conduct*, and as such must be legal constructs on the same conceptual continuum, or spectrum.[80] Thus, proving irrationality would for all practical intents and purposes (specifically in terms of evidence and argument in litigation) be tantamount to proving a unreasonableness that very, very closely resembles gross negligence.

(c) Impact

The conclusion of this analysis is that for practical purposes — on a spectrum of conduct between excessive reasonableness and the most extreme gross negligence — the business judgment rule's 'rationality' encroaches far enough onto the territory traditionally inhabited by (the duty of care and skill's unique form of) reasonableness, for it to have reduced the scope of liability to something that closely resembles a related but much less stringent legal construct — gross negligence.[81] The net effect is that the ambit of the duty of care and skill has been reduced to something close to its earliest English law form.[82]

An important question is thus: is there some hidden or implicit policy basis that explains why directors should be excused from the ordinary

[79] *Transnet Ltd t/a Portnet* paras 290–291.

[80] They are indeed recognised as such in, for instance, the field of administrative law for the purposes of judicial review.

[81] See Cassidy, (2009) 20 *Stell LR* 373 at 399–400 for commentary to the same effect, and support for the overall analysis found above.

[82] See above at 4 and n16.

principles of the law of delict when, for example, they are not professionals such as auditors or attorneys? Far more importantly, however, is the following: if the standard for liability is then in fact for all intents and purposes akin to gross negligence, does the test for the duty of care and skill then actually differ from the test for s 22(1)'s acquiescence to recklessness, which requires at a minimum gross negligence? Or, if one can not go as far as that, does this state of affairs not to some degree (i e in cases of insolvency) render the care and skill remedy defunct, as it becomes more difficult to pursue than an action based on the reckless carrying on of business?

III RECKLESS TRADING

In this section, directors' liability for 'reckless trading'[83] in the current Companies Act, as well as the applicable provisions of its predecessor, will be examined.

It considers whether, in some respects, the reckless trading provision provides potential company-litigants a better remedial avenue for holding a director or directors liable once a company is insolvent than does the action for breach of duties of care and skill as outlined above.

(a) The provision's meaning

This section aims, as stated, to examine the proper construction of the statutory action for reckless trading. In so doing, it will briefly analyse the provision's history, the treatment given to it by the courts, and its indirect reliance on certain delictual constructs. Thereafter, in the following section, the two remedies will be compared.

The Companies Act 46 of 1926 did not contain a reckless trading provision. In 1939, s 185*bis* was inserted into the Act. This provision was the forerunner of the reckless trading concept found in modern company law, but was severely limited in scope: it did not go as far as to include recklessness, and applied only to trading once a company was in judicial management or the process of winding up.[84] 'Reckless' trading itself was only introduced in s 424 of the Companies Act 61 of 1973, as above, applying to 'winding-up, judicial management *or otherwise*',[85] indicating that the remedy was from then on also available whilst the

[83] It is important to note that here the focus is on reckless trading, rather than fraudulent trading.
[84] *Philotex (Pty) Ltd* para 142G.
[85] Not to be given a euisdem generis interpretation [own emphasis].

company remained a going concern.[86] This seems to have been in order to 'extend the remedy by means of which a restraining influence can be exercised on "over-sanguine directors."'[87] The most authoritative case in South Africa in this regard remains *Philotex (Pty) Ltd v Snyman*.[88]

Liability for reckless trading is neither contractual nor delictual but statutory in nature. It must be proved that a director 'acquiesced in the carrying on of the company's business despite knowing that it is conducted in a manner prohibited by section 22(1)',[89] ie at least in a reckless manner. Under the current Act, '*knowing*', '*knowingly*' and '*knows*'[90]

> 'when used with respect to a person, and in relation to a particular matter, means that the person either-
> *(a)* had actual knowledge of the matter; or
> *(b)* was in a position in which the person reasonably ought to have —
> (i) had actual knowledge;
> (ii) investigated the matter to an extent that would have provided the person with actual knowledge; or
> (iii) taken other measures which, if taken, would reasonably be expected to have provided the person with actual knowledge of the matter'.

Further, '*acquiesce*' means '[t]o agree, esp. tacitly; to accept something, typically with some reluctance; to agree to do what someone else wants; to comply with, concede'.[91]

The wording of s 424, on the other hand, read that a director may not be 'party to' reckless trading. In the *Philotex* case, the court held that 'being party to' does not involve 'the taking of positive steps in the carrying on of the business; it may be enough to support or concur in the

[86] Cassim (ed) et al, (Juta 2012) 588.
[87] *Philotex (Pty) Ltd* para 142H.
[88] *Philotex (Pty) Ltd* para 142H. For a detailed discussion of the judgment, broadly in keeping with the observations made below, see Havenga, 'Director's personal liability for reckless trading: Philotex (Pty) Ltd v Snyman, Braitex (Pty) Ltd v Snyman 1998 2 SA 138 (SCA)' (1998) 61 *Tydskrif vir Hedendaagse Romeins-Hollandse Reg* 719.
[89] Section 77(3)*(b)* of the Act.
[90] Section 1.
[91] *Oxford English Dictionary* 3 ed (2011).

conduct of the business ...'.[92] Thus it is submitted that this aspect of the test is probably in principle no different to section 424 of the 1973 Act.[93]

It is unsurprising that most, if not all, cases dealing with reckless trading do so in the context of insolvency. It would seem, also, that to trade recklessly in this context is to trade whilst being *commercially* insolvent. This makes a great deal of sense, as it would be at odds with commercial practice for companies, who for example often trade on credit, to be unable to trade when technically insolvent by virtue of the rule.[94]

However, if the requirements for proving reckless trading are satisfied, a director is, as per s 77(3)*(b)*, liable for any '... loss, damage, or costs sustained by the company as a direct or indirect result of ...' the director's knowing acquiescence to the transaction, or series of transactions. In essence, the inquiry hinges again on the standard of conduct set by the Act.

(b) Select aspects of importance: negligence and causation

(i) Recklessness and negligence

The starting point for an understanding of the development of the 'negligence' portion of the test for reckless trading is *Howard v Herrigel and another*.[95] Therein one finds the following:[96]

> '... [T]he applicant must prove, on a balance of probabilities, that the person sought to be held liable had knowledge of the facts from which the conclusion is properly to be drawn that the business of the company was or is being carried on recklessly ... It would not be necessary to go further and prove that the person also had actual knowledge of the legal consequences of those facts.'

It constitutes a purely objective test for recklessness, capable of being influenced only by external factors,[97] and was further confirmed in both

[92] *Philotex (Pty) Ltd* para 143, and see also *Howard v Herrigel* 1991 (2) SA 660 (A) para 674H; and Havenga, (1998) 61 *THRHR* 719 at 720.

[93] See also Van der Linde, 'Personal liability of directors for corporate fault — An exploration' (2008) 20(4) *SA Merc LJ* 439 at 443.

[94] Cf for example, Cassim (ed) et al, (Juta 2012) 590 or 'The New Companies Act: Peculiarities and anomalies' (2009) 126(4) *South African Law Journal* 806 at 812.

[95] *Howard* para 674H.

[96] *Howard* para 673I–674H.

[97] *Howard* para 678C–E, stating that:

> '... the legal rules are the same for all directors. In the application of those rules to the facts one must obviously take into account, for example, the factors referred to in the judgment of Margo J in the *Fisheries Development* case and any others which

Ozinsky v Lloyd and others,[98] and *Ex Parte Lebowa*.[99] Throughout this line of cases, it was held that a company that continues to incur debts when the reasonable businessman would be of the opinion that there would be no reasonable prospect of paying the creditors when the debts are due, is considered to be trading recklessly.[100]

However, the *Philotex* case — the locus classicus regarding 'reckless trading' in South Africa — deviates from this approach in setting out the definitive test for recklessness, and brings the inquiry closer to the subjective-objective dichotomy exhibited by the standard prescribed by the duty of care and skill. First, it states that the test remains partially objective, because a person's conduct is measured against the standard of conduct of the reasonable person. The subjective belief of a director as to whether payment could be made is neither conclusive, nor relevant if the reasonable business person in the same circumstances would not share such a belief.[101]

Second, however, the court rules that the test is also partially subjective — one still has to measure the conduct against what is expected of people moving in the same sphere as (i e comparable to), and having the same knowledge or access to knowledge as the person in question.[102] In keeping with the *Howard* case, the inquiry also examines external factors including, among others, the scope of the business of the company, the role, functions and powers of the directors, the debts, the extent of the financial difficulties of the company and the prospects of recovery.[103]

The court's most important contribution, however, is its treatment of the recklessness-concept itself. First, the court confirms that it involves at least an element of *risk*, regardless of whether the defendant is subjectively aware thereof.[104] Second, as to the relationship between 'recklessness' and 'negligence', it makes a number of crucial observations.

may be relevant in judging the conduct of the director. His access to the particular information and the justification for relying upon the reports he receives from others, for example, might be relevant factors to take into account, whether or not the person is to be classified as an "executive" or "non-executive" director.'

[98] 1992 (3) SA 396 (C).

[99] *Development Corp Ltd* 1989 (3) SA 71 (T).

[100] *Ozinsky* paras 414G–H.

[101] *Philotex (Pty) Ltd* para 147.

[102] *Philotex (Pty) Ltd* para 143; Havenga, (1998) 61 *THRHR* 719 at 720, and De Koker, 'Roekelose of bedrieglike dryf van besigheid — 'n verdure hoofstuk' (1995) 20 *Tydskrif vir Regswetenskap* 101 at 114–117.

[103] *Philotex (Pty) Ltd* para 144; see also Bekink, (2008) 20 *SA Merc LJ* 95 at 101.

[104] *Philotex (Pty) Ltd* para 143.

S v Van Zyl[105] held that recklessness included gross negligence. This was confirmed in *S v Dlamini,*[106] where it was stated that reckless conduct was a failure to consider the consequences of an action. This implies an attitude of 'reckless disregard of such consequences'.[107] However, with reference to *Ozinsky v Lloyd*,[108] *Philotex* clearly distinguishes recklessness (including gross negligence) from mere negligence.[109]

As per the court, in the context of conducting business (specifically, for instance, the borrowing of money under insolvent or near-insolvent circumstances) the distinction would be as follows. If the reasonable businessman, despite believing that a company has a chance of paying its creditors, would refrain from running a particular risk because of circumstances which create a material but not high risk of non-payment, a director who does run that risk and incurs credit is acting unreasonably and therefore negligently. Nonetheless, such conduct would not be characterised as recklessness, and thus is not grossly negligent. Gross negligence, on the other hand, would be where the reasonable business person would know that non-payment was a 'virtual certainty'.[110]

The latter, however, is an extreme form of recklessness, and there is some middle ground. If, objectively speaking, there was a 'strong chance' of non-payment, the test for liability would also be satisfied, and '[i]t is not possible to attempt to draw the line between negligence and recklessness more exactly. Each case must turn on its own facts and involve a value judgment on those facts'.[111] What is clear from *Philotex* is that gross negligence is at least the de facto standard of conduct for determining recklessness.

Therefore, at present, the quasi-delictual negligence inquiry within the reckless trading provision remains one that takes into account the subjective characteristics of directors. Nonetheless, what directors lose on the swings, they gain on the roundabouts, as liability is, essentially, confined to gross negligence or something very similar.

(ii) Causation

It is trite that causation will have to be proved for liability for the breach of the duty of care and skill. Is this also required for reckless trading?

105 1969 (1) SA 553 (A) paras 559 D–G.
106 1988 (2) SA 302 (A) paras 308D–E.
107 *S v Dlamini* paras 308D–E.
108 See n98.
109 *Philotex (Pty) Ltd* para 143.
110 *Philotex (Pty) Ltd* paras 146–147.
111 *Philotex (Pty) Ltd* para 147.

In *Philotex* the court held that 'a director can be held personally liable for liabilities of the company without proof of any causal link between his conduct and those liabilities'.[112] However, in *L & P Plant Hire BK v Bosch*,[113] the court seemingly held that there had to be a causal link between the reckless conduct and the close corporation's inability to pay.[114]

From *Saincic and others v Industro-Clean (Pty) Ltd and another*,[115] it would appear that the Supreme Court of Appeal confirmed the *L & P Plant Hire* dicta in the context of causation required in terms of section 424. In this respect, the court stated[116]

> '... that as far as creditors are concerned there must be some or other causal link between the fraudulent conduct and the inability to pay the debt. In other words, it must be due to the fraudulent conduct that a particular creditor's debt cannot be repaid.'

However, the Supreme Court of Appeal clarified the meaning of this dictum in *Fourie v FirstRand Bank Ltd*,[117] stating:[118]

> 'The context of *L & P Plant Hire* was that there was no evidence that the close corporation concerned was unable to pay its debts. Read in that context, the judgment is rightly understood ... as saying no more than this: if, despite the reckless conduct of the company's business, it is nevertheless able to pay its debt to a particular creditor, that creditor has no cause of action under s 64 — or s 424 — against those responsible for the reckless conduct.'

Thus, it held that:[119]

> '*L & P Plant Hire* was never intended to deviate from those decisions of this court (such as [*Howard* and *Philotex*]) which expressly laid down the general principle that s 424 does not require proof of a causal link between the relevant conduct and the company's inability to pay the debt. ... *Saincic* recognised an exception to this general principle where the converse had been positively established, namely that there was plainly no causal connection between the relevant conduct and the debt . . .'.

This renders the matter essentially above the level of dispute — causation, in short, is a factor to be considered, but no cause of action

[112] *Philotex (Pty) Ltd* para 142.
[113] 2002 (2) SA 662 (SCA).
[114] *L & P Plant Hire BK* paras 39 and 40.
[115] 2009 (1) SA 538 (SCA).
[116] *Saincic* para 29.
[117] 2013 (1) SA 204 (SCA).
[118] *Fourie* para 28.
[119] *Fourie* paras 30–31.

will stand or fall on its presence or absence from a particular set of facts *unless* the company is seemingly able to pay its debts, or there is no relationship whatsoever between the reckless conduct and the company's (therefore unrelated) inability to pay.

The new Act, with its inclusion of 'as a direct or indirect result' in s 77(3), maintains the same broad approach, concretising the matter only as far as to say the loss must be in some way connected to the recklessness. An 'indirect result' is most certainly couched widely enough to include cases where causation is less than definitive. One cannot find fault with the reasoning in the above judgments, and it would certainly be overly restrictive to interpret the new provision as narrowing the scope of the remedy via stricter causal requirements. In sum, therefore, it would be accurate to say that whilst some 'cognisable link' between the conduct and commercial insolvency is necessary, it does not require in all cases a stricter 'causal link'.

IV CRITICAL PERSPECTIVES

In this section, a number of critical perspectives, based on the preceding analysis are presented. This is centred on the practical effects of the remedial dispensation effected by the Companies Act, and whether these effects are in line with the policy principles that lie behind those provisions. This is done with respect to (1) companies approaching the point of liquidation — i e insolvent but still trading; and (2) companies beyond the point of liquidation, where the 1973 Companies Act remains applicable.

(a) Insolvent, but not in liquidation: remedial consequences

(i) The perspective of the company

As seen above, the courts have held in the context of the reckless trading provisions that recklessness includes gross negligence as a *minimum* standard, and that there is nothing to distinguish 'recklessness' per se from 'gross negligence' except that the former can exceed the latter. Furthermore, it has been argued in § II*(b)*(ii) and § II*(c)* that under the regime of the current Companies Act, the standard of conduct in cases of breach of the duty of care and skill has been so attenuated by the business judgment rule that effectively what is required to be proved to hold directors liable for a breach of the duty of care and skill is the practical equivalent of gross negligence.

This is a significant aspect of the new Companies regime. To grasp the full effect, regard must be had for the effect of s 77. Both s 77(2)*(a)*[120] and (3)*(b)*[121] make it clear that a director may be held liable '...for any loss, damages, or costs sustained by the company ...'. Historically, the company has always had, and continues to have, a remedy for breach of the duty of care and skill available to it. However, this has not always been the case regarding the remedy for reckless or fraudulent trading.

The approach is, in fact, a radical departure from the predecessors of s 22(1) in the Companies Acts of both 1926 (s 185*bis*) and 1973 (s 424), of which the company itself was unable, whilst a going concern, to avail itself.[122] For the first time in South African company law, the company itself is provided with recourse against its directors for their part in the company having been allowed to carry on its business in this prohibited manner. Therefore, should a company which is *insolvent but not in liquidation* want to hold one or more of its errant directors liable for putting it in this position, it would effectively have a choice between litigating on the basis of reckless trading or a breach of the duty of care and skill.

In § II*(c)*, the question of whether these two remedies practically differ was posed. It is trite that they do not share an Aquilian character, and that only in actions for breach of care and skill must all five delictual elements be satisfied. Specifically, the remedy based on s 22(1) requires neither the burden of attributing some dimension of objective unreasonableness to the state of affairs in question ('wrongfulness'), nor necessarily a full exploration of the causal effects of the defendant's conduct for it to be successfully utilised.[123] This raises the question of why a plaintiff-company would choose to enforce the duty of care and skill. From the perspective of litigation, a company would be burdened with a more difficult and complex case, requiring more to be proven than in pursuing liability on the basis of reckless trading. The submission made here is that it is far more likely in future that companies in such circumstances will make use of the latter, rather than the former, to recoup its losses from directors.

[120] Governing liability for, inter alia, a breach of the duty of care and skill.

[121] Governing liability for, inter alia, contravention of s 22(1), the reckless or fraudulent trading provision.

[122] The 1926 provision provides this remedy to '... the Master, or the liquidator or any creditor or contributory to the company ...', and the 1973 provision adds to these person also '... the judicial manager ... [and] ... any member ... of the company ...'. It is in neither statute extended to the company itself in a manner comparable to the remedies for breach of the fiduciary duties or duty of care and skill.

[123] Kennedy-Good & Coetzee, (2006) *Obiter* 277 at 281.

(ii) Creditor protection: a counter-intuitively positive policy shift

In light of the above, the crucial issue in terms of the Act is its impact on creditor protection.

From the perspective of a creditor, as a company steadily approaches the point of liquidation, it will be of utmost importance to institute proceedings as soon as possible. This is in order for him to obtain and execute judgment before formal winding-up and pre-emptively circumvent the concursus creditorum. However, the Act seemingly bars a creditor from utilising s 22(1) to protect its interests. That is not the manner in which the Act has been interpreted to date, but it is argued that the currently prevalent interpretation is not correct.

According to a number of current authorities,[124] the only manner in which a creditor would be able to institute action for the recovery of losses as a result of reckless or fraudulent trading is through the operation of s 218(2), which states that

> '[a]ny person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention'.

It is certainly uncontentious to assert that the historic policy-basis of this remedy has been creditor-protection. Section 185*bis*(1) of the 1926 Act and s 424(1) of the 1973 Act explicitly state that '[i]f ... it appears that any business of the company has been carried on . . .' (in terms of the latter Act only is added '... recklessly or ...') '... with intent to defraud *the creditors of the company or creditors of any other person* or for any other fraudulent purpose ...',[125] the remedy is activated. Section 185*bis* holds 'any of the directors, whether past or present' liable, whilst s 424(1) holds 'any person' liable.

The remedy clearly functioned as counter-balance to the corporate form, through which individual creditors were able to recoup their losses in instances where, due to the operation of both juristic personality and limited liability, they otherwise could not.

In contrast, s 22(1) chooses to do away with specific reference to creditors, substituting the italicised phrasing above with 'any person'. Furthermore, s 22(1) is not the full operative extent of the Act's arrangements regarding reckless or fraudulent trading. It has been fragmented, and partially placed also in s 77(3)*(b)*. Nonetheless, in

[124] Such as Wainer, (2009) SALJ 806 at 812; Cassim (ed) et al, (Juta 2012) 587, 589; Delport & Vorster (eds), *Henochsberg on the Companies Act 71 of 2008* (LexisNexis, Service Issue 10, 2015) s 22; and *Rabinowitz v Van Graan* 2013 (5) SA 315 (GSJ) para 18.

[125] [Own emphasis].

Rabinowitz v Van Graan and others,[126] the court made two very important observations in this context.

First, the court held that it is in principle correct that if a director is found to have acted in conflict with s 214(1)*(c)*,[127] such a director has 'contravened the Act', thereby activating the provisions of s 218(2).[128] This may or may not be correct. It is difficult to see how the latter provision, which exists to supplement the civil liability dimension of the Act, can be brought into operation by a provision existing specifically to govern the *criminal* liability paradigm of the Act. The basic argument advanced here is that a 'contravention' of the Act for the purposes of s 218 must be read to mean a contravention of the Act's civil provisions only. It is, however, in line with a literal interpretation of the Act, and as the primary focus of this article is on reckless, rather than fraudulent, trading, the point is not pursued.

Second, after citing various contemporary authorities that reach the same conclusion,[129] the court holds that in view of the delinquency provisions in s 162(5)*(c)*, the criminal liability provisions in s 214, and the express liability in favour of the company found in s 77(3)*(b)*, it cannot be the case that the legislature intended to exclude individual creditors from seeking remedial action for a contravention of s 22(1).[130] As pointed out, this is in line both with the legislative history of s185*bis* and s 424 of the previous Companies Acts respectively. Prima facie, it does indeed seem unreasonable that an individual creditor is unable to hold directors personally liable for their role in a company's reckless trading.

Nonetheless, it is submitted that the Act has indeed barred creditors from instituting action on the basis of s 22(1), for a number of reasons. These reasons fall into two main categories: interpretive issues, and arguments based on the plaintiff of preference[131] principle, operating in conjunction with the salient policy principles underlying the protection of creditors.

[126] See n124.

[127] Section 214(1)*(c)* reads: 'A person is guilty of an offence if the person...was knowingly a party to any act or omission by a company calculated to defraud a creditor or employee of the company, or a holder of the company's securities, or with another fraudulent purpose ...'. The action *in casu* was instituted for *fraudulent* trading, which is the 'offence' in question. It is crucial to note that this section, unlike s 218, includes the elements of knowledge and participation.

[128] *Rabinowitz* paras 13–17.

[129] *Rabinowitz* paras 18.1, 18.2.

[130] *Rabinowitz* paras 20, 21, 22.

[131] A formulation preferred here over the more often used terminology of 'proper plaintiff' or 'proper claimant' as derived from *Foss v Harbottle* (1843) 2 Hare 461, 67 ER 189.

A. The interpretive difficulties of s 218 in the context of s 22(1):

The wording of s 218 makes it clear that a *provision* of the Companies Act must be *contravened* for it to provide an injured party with a remedy. The first question that therefore arises is whether all the Act's provisions can be 'contravened'. Clearly not — for example definitional,[132] interpretive[133] or any other type of provision that is not peremptory or substantially directory are *hermeneutically* incapable of being contravened. In contrast, any provision which is by nature prescriptive or in some way regulates conduct is capable of contravention.

Thus, it is clear that s 22(1) can be contravened — *but only by the company itself*, as the section prescribes what the company itself may and may not do.[134] Section 218(2) recourse against the juristic person (which indeed seems hermeneutically possible) is, of course, practically moot as judgment creditors do not obtain a preferential position in the concursus. More importantly, if put differently: any one or more of the directing minds with the power to act 'as the company' cannot, when acting as the company,[135] personally contravene s 22(1). Whilst a director is unable to contravene s 22(1), the conduct of directors *in relation to* s 22(1) is governed by s 77(3)*(b)* as above. The salient question, then, is whether a director may contravene the latter section by knowingly acquiescing to the company's contravention of the former.

Yet, in contrast to s 76, the section does not operate prescriptively — its wording merely empowers the company to hold directors liable for conduct delineated therein. Therefore, a creditor can neither argue that a director contravened s 22(1), nor s 77(3)*(b)*, and certainly not that a person 'contravenes any provision of this Act' merely by acting in a manner that exposes *that same person* to liability towards the company in terms of the Act. It is fundamental to remember that in this context, when one speaks of holding 'a director liable' it means holding a director *personally* liable.[136]

That, however, is not the end of the inquiry. Whilst s 77(3)*(b)* can itself not hermeneutically be contravened, it is probably correct to state that the section tacitly imposes on directors an *implicit duty not to knowingly acquiesce* to the company carrying on its business in a

[132] Such as s 1 or s 43(1).

[133] Such as s 7.

[134] It is important to note that whilst a creditor may surely use s 218 to found a claim *against the company* for a 'pure' breach of s 22(1), that would not confer any advantages in terms of the overall concursus creditorum.

[135] Such that, constructively, the company itself is acting.

[136] Thus, even if a single director has the power to act as the company and does so recklessly or fraudulently, the director him- or herself is not contravening s 22(1); the company is.

'reckless' manner. One could argue, therefore, that a creditor could utilise section 218(2) by averring that the contravention in question was acting in conflict with this implied duty imposed by the Act.

Unfortunately this argument also cannot aid a creditor-plaintiff with a cause of action, as it omits the question of to whom that implicit duty is owed. Section 22(1) imposes a duty on the company, towards 'any person', but *only* empowers the company itself to assert its co-relative right against its own directing minds — via s 77(3)*(b)*.[137] Why?

Section 22(1) provides a standard of conduct for the company, and s 77(3)*(b)* identifies those persons who have played an actionable part in (1) the company acting in conflict with that standard, (2) to its own detriment. Thus in order to allow the company to proceed in effect against its own directing minds, s 77(3)*(b)* imposes a *subsidiary duty towards the company* upon those minds — its directors — in order to give effect to that standard.

The premise of this 'loop of liability' is the violation of a standard of conduct imposed on the company (to the benefit of third parties), but it is the consequent harm done by the company to itself that actuates it (as is the case with the entire s 77). The insight from this analysis is that the subsidiary duty of the directors — not to acquiesce — is owed not towards 'any person', but rather toward the company itself only. Therefore a creditor cannot argue that s 218(2) has been activated on this basis — the duty not to acquiesce knowingly is not owed toward creditors, and breach of this duty can found no cause of action in favour a creditor-plaintiff.

B. The company as the plaintiff of preference: a policy analysis

In addition to the interpretive argument, it is submitted that there are legal policy reasons why this seemingly 'radical' interpretation should stand. In essence, the argument advanced is that it is in the best interests of creditors that the company itself remain the plaintiff of preference in actions concerning s 22(1).

It is a well-established principle of company law that shareholders enjoy primacy among the group of stakeholders in companies, and therefore enjoy the benefits not only of certain governance rights, but also of various protective legal mechanisms to safeguard against agency-risks inherent in the separation of ownership and control. This enjoyment is definitively to the exclusion of the company's creditors whilst a

[137] A quirk of juristic personality which, as is argued below, is underpinned by a very sound policy basis.

going concern. However, it is another fundamental principle of company law that the interests of creditors enjoy primacy over shareholders regarding companies' debts, such that in principle, shareholder-creditors usually stand last in the queue of creditors, and more importantly, that shareholders are entitled to the residual assets of the company only after all liabilities have been dealt with.

It is further uncontentious that the mischief informing s 22(1) is: actions by the company, taken in a objectionable manner, to the detriment of its stakeholders — in light of the provision's history, *especially* its creditors. It has also been argued that as a company approaches 'the zone of insolvency', there is also a definitive shift in emphasis regarding the duties of directors, and the interests of the company's creditors gain ever-increasing significance.[138] Therefore, the central question becomes *how*, rather than whether, to protect the company's creditors against these kinds of abuses.[139]

Beginning with *Salomon v Salomon and Co Ltd,*[140] through the construct of juristic personality, limited liability firmly entrenched the internal inviolability of the company as a sovereign economic unit. As a matter of enduring principle, creditors (and other stakeholders) were thereby placed on the far side of the so-called corporate veil.[141] Yet the remedy for reckless trading allows individual creditors to disregard the corporate veil and hold directors personally liable. Are there compelling theoretical positions to justify a departure from this principle when reckless trading has been allowed to occur?

Legal-economic perspectives of the company (or the 'firm'), which are highly influential in determining the policy basis for company legislation, provide a number of normative insights into how such a remedy *ought* to operate. The influential 'nexus of contracts' theory of Jensen and Meckling posits the reduction of economic transaction and monitoring costs as the central function of the standardised corporate form.[142] By functioning as a counter-measure to juristic personality, the

[138] Rajak in 'Director and officer liability in the zone of insolvency: A comparative analysis' (2008) 1 *Potchefstroom Electronic Law Journal/Potchefstroomse Elektroniese Regsblad* 1 at 25–30.

[139] See also Sigwadi, 'Personal liability for the debts of close corporations: case comments' (2003) *SA Merc LJ* 303 as in the context of s 424 of the 1973 Companies Act; and Rajak, (2008) *PER* 1 at 23–25; and in terms of all stakeholders, see Esser & Du Plessis, 'The stakeholder debate and directors' fiduciary duties' (2007) 19 (3) *SA Merc LJ* 346 at 350–351.

[140] *Salomon v Salomon* [1897] AC 22 para 52.

[141] In this regard, see also the comments of Rajak, (2008) 1 PER 1 at 1–10, where 'the financial burden of corporate failure would be thrown on to the creditors' (at 8).

[142] See most importantly Jensen & Meckling, 'The theory of the firm: Managerial behavior, agency costs, and ownership structure' (1976) 3 *Journal of Financial Economics* at 305.

reckless trading remedy undermines this, and must (like all instances where the corporate veil is ignored) therefore be shown to advance the cause of economic efficiency further by disregarding the internal inviolability of the corporate form, than by upholding it. It does not.

It is submitted that one of the most important reasons such a nexus of contracts (in the economic sense) is coalesced into a juristic person[143] is the parity of creditors (and additional mechanisms for their protection) it achieves in order to compensate for the trade-off of limited liability. This is supported by subsequent theoretical developments that argue that the corporate form functions as more than a specialised and standardised legal nexus of contracts that reduces transaction and other economic costs.

Specifically, as argued by Hansmann and Kraakman, it serves a crucially important, *creditor-centric*, economic function — the 'partitioning of assets'. Where managers' and owners' assets are partitioned off from those of the company, it allows creditors to conclude far more economically efficient contracts. Assets are not only separate but also partitioned through limited liability — thus creditors are placed in a much better informational position from which to make judgment-calls regarding the terms on which to extend credit. This greatly improves the economic efficiency and risk dynamics of lending — both to the aforementioned individuals, and their companies respectively and separately.[144]

But more importantly the same reasoning also applies between creditors of the company *amongst themselves*. How are potential creditors accurately to determine the most efficient terms of credit if it is uncertain whether other creditors will (on the cusp of liquidation) undermine the integrity of this partition by piercing the corporation veil? It hampers the ability to make sound economic judgments. As such, juristic personality (as a legal construct) is shown to be more than a descriptive heuristic for the legal means whereby economic cost-reduction is achieved.

In this light, one of the central tenets of juristic personality gains renewed significance — the ability to sue in own name. In essence the argument advanced here is that, by allowing a company to sue in own name, it allows that company to absorb any losses it may have suffered from errant conduct (whether committed internally or by third parties)

[143] In other words, the 'firm' as a co-ordinating third entity representing a contractual locus through which business is organised — Hansmann & Kraakman, 'Organizational law as asset partitioning' (2000) 44 *European Economic Review* 807 at 808–809.

[144] Hansmann & Kraakman, (2002) *EER* 807 at 810–812.

and *return the quantum of loss to the partitioned group of assets.* This restores the parity of creditors that partitioning brings about, facilitating the efficient allocation of credit, as well as the fair distribution of harm. This policy perspective redoubles the fundamental importance of the plaintiff of preference principle, as derived from *Foss v Harbottle*[145] — it protects the company's ability to recoup its own losses first, to the exclusion of third parties (including its owners).

This is the cause of the development of the 'derivative action'. *Foss v Harbottle* also provides the doctrinal perspective underlying the derivative action (now contained exclusively in s 165 of the Act) — namely, when a company is harmed, the company itself must be allowed to litigate *first* to recover those losses, unless the contrary can be proven, in which case litigation can be undertaken on the company's behalf.

This perspective is further supported by the approach in *Fundstrust v Van Deventer,*[146] which further emphasises the sanctity of corporate personality, and by implication the primacy of the company's right to sue, and be sued, (first) in own name. The court specifically stated that any liability imposed on directors (and therefore which '[impinges] on the corporate existence') should be interpreted strictly. Importantly, this statement was made within the context of personal liability of directors in *personal liability companies*, which makes the point even more compelling in the context of ordinary companies, where such 'corporate existence' is more strongly enforced.

The outlined theoretical perspectives on the firm reveal an overarching policy-basis that informs the doctrinal position evidenced by these two cases, and further justifies the integrity and inviolability of the legal and economic unit (the company). The law protects the ability of the company to preserve its economic integrity to the exclusion of others, because the internal arrangements inherent to that 'partitioned' economic unit of assets (i e arrangements within the nexus of contracts) will adequately discount the corresponding benefits amongst its stakeholders. The underlying assumption is inviolable:[147] that corporate form (juristic personality with limited liability) is a *correctly calibrated* institution, which accurately accounts for the constellation of interests and interest-clusters it brings about. Creditors' harm (which is *indirect*, flowing from the harm of the company — for example through reckless trading) must only be actionable if one can say with certainty that the

[145] See n131.

[146] *Fundstrust (Pty) Ltd (In Liquidation) v Van Deventer* 1997 (1) SA 710 (A).

[147] Seeing as to do away with it requires a complete re-evaluation of the policy basis for separate juristic personality in the first place.

company is not in the best position to discount that harm amongst its various stakeholders, specifically its body of creditors.[148]

This brings one to the operation of s 424 of the 1973 Companies Act. This section, unlike its predecessor, applied not only to companies in judicial management or winding up, but also whilst the company remained a going concern. The section explicitly made *creditors*, among others, a plaintiff of preference, and excluded the company from bringing this action against its directors.

The context of this section's analysis is companies that are insolvent but not yet in liquidation. Thus consider the effects of s 424: as the company approaches or surpasses the point of insolvency (and is in all likelihood approaching formal liquidation) it effectively allows one or more of the overall body of creditors to obtain judgment against errant parties (first and foremost the directors) within the company, holding them personally liable, before the liquidation process is initiated.

The implication is that, if successful, it will in most cases reduce these judgment-debtors to men of straw. The eventual liquidators will be unable to recover any meaningful amount from them through liability they may owe the company due to their recklessness (such liability is also likely). Thus it reduces the company's ability to recoup related losses from these individuals through remedial avenues such as breach of fiduciary duties, or the duty of care and skill.

As a consequence, first, the amount the overall body of creditors will eventually receive is reduced, to the detriment of the concursus as a whole. Second, it allows the litigating creditor to drink twice from the well — first from those 'party to' the recklessness personally, and second from the company after winding up. Third, it favours the biggest and strongest creditors, for whom it will be comparatively easier to undertake such (expensive and burdensome) litigation. In contrast, the weaker creditors (arguably those in greatest need for protection) suffer as a result.

By supplanting the company with its individual creditors as the preferential plaintiff, s 424's policy stance confused the protection of individual creditors with the broader principle of creditor protection. In reality, it created the potential for harm to the body of creditors as a whole, to the benefit of the few who are able to 'skip the queue' via the operation of s 424.

[148] It is important to note, however, that there is a difference between asserting that the corporate form is a 'correctly' calibrated institution and asserting it is a *perfectly* calibrated institution — if the latter was the case, there would be no need for supplementary creditors' remedies whatsoever.

In contrast to its predecessors, s 22(1) of the new Act functions to correct this. In conjunction with s 77(3)*(b)*, it gives the company status as plaintiff of preference, allowing it to recover the losses it has suffered from the responsible parties — its directors. In so doing, it allows the company as judgment-creditor to absorb the quantum of harm in own name, restore it to the partitioned assets, and use it for the benefit of the concursus as a whole. Whether as consequence the company is in a position to pay its debts to its body of creditors and avoid liquidation, or must still face formal winding up, it will (in line with the principle of primacy of creditors in matters of company debts) be able to spread the proceeds amongst all its creditors equally.[149] This restores the parity of treatment on which the economic efficiency of creditors' evaluations of future transactions is based, whilst still retaining the deterrent and punitive functions of the remedy.

Seen as such, three points could be argued. First, the company (even in liquidation, but more so if insolvent yet still a going concern) is indeed in the best position to discount the interests of the body of creditors as a whole, and to effect a fair and equal repayment of its debts. If this is not accepted, the implicit concession is that the company is not a correctly calibrated institution for the discounting of benefits and losses to its stakeholders. Thus it cannot form the point of departure, and the burden to show otherwise should thus fall on the creditor-plaintiff when making use of an appropriate remedy.

Second, as a result of this submission, showing why the company is the plaintiff of preference, it is argued that s 218(2) must be interpreted restrictively, so that it does not impair the company's ability to do so (at the expense of a portion of the concursus). Reading it widely, as leading authorities seem to do,[150] would allow individual creditors to subvert the proper and fair ranking of the company's debts by taking action against the directors directly. Such action would weaken the company's ability to collect compensation from internal transgressors and divide it equally amongst harmed third parties. It must not be forgotten that

[149] This approach is also broadly in keeping with s 22(1)'s equivalent in the United Kingdom's Insolvency Act of 1986, which empowers the company itself (albeit through the liquidator) to hold a creditor liable, rather than the creditors themselves. See also Rajak, (2008) 1 *PER* 1 at 21–23.

[150] See for instance Cassim (ed) et al, (Juta 2012) 589 and 858 (although, with respect, without any analysis as to *why* this interpretation is the correct one); or Delport & Vorster (LexisNexis 2015) 124 at s 22 and s 218 (where the same critique applies). It seems that the wording of s 218 is, generally, taken at face value, without regard for a policy-basis for how it ought to be read, nor any inquiry into its hermeneutic interaction with the provisions, which ostensibly activate its operation (the subject of the next section).

when a company trades recklessly, it does so at the peril of *all* creditors equally.

Therefore, specifically in light of what underlies the principles evidenced by *Foss* and *Fundstrust*, in order for s 218(2) to have allowed creditors to so disregard the corporate veil, there must be a compelling reason. For instance, to rebut the interpretive issues, there should be something more within the Act (which there is not), or perhaps there should have been something more to s 218(2) to link it to the s 22(1) and s 77(3) remedy. Without amendment, the section cannot allow it. Moreover, the policy-based arguments show that it would in any event not be a desirous outcome. In fact, the only point favouring the currently accepted view in favour of creditors' access to this remedy is the workings of s 22(1)'s antecedents, and it is submitted that reliance on past principles, without more, is not enough.

Third is the question of whether such an interpretation leaves creditors without effective recourse in cases where it would indeed be justified for them to hold directors personally to task for causing harm to their interests in the company. Should this be the case, then the demands of commercial exigency ought to trump both the interpretive and policy-oriented arguments made above. Yet this is not the case.

In the first instance, there is nothing preventing creditors, jointly or severally, from bringing a true derivative action in terms of s 165(2)*(d)* on behalf of the company against directors who have caused the company to trade recklessly. Through such an action, litigant-creditors improve the position of the concursus of which they are members. It would be difficult, especially as a company approaches the 'zone of insolvency', for a court to deny that such action is either 'necessary or expedient' to protecting the rights of the plaintiffs — by acting on behalf of the concursus at large, these creditors indirectly protect their own rights.

Also, action can be brought by creditors for a breach of the duty of care and skill, via s 218(2). It has been argued above that s 76 of the Act is indeed capable of contravention, and presents no problem to the founding of a cause of action in terms of s 218(2). This is perhaps the most surprising outcome of this analysis. To some extent, the duty of care and skill and the prohibition on reckless or fraudulent trading have, from a remedial perspective, *actually reversed roles.* Whilst it has been shown that a company will in all likelihood use the less burdensome requirements of s 77(3)*(b)* to recover its losses from errant directors, the company *creditors*' path of least resistance has become recourse to the duty of care and skill via s 218(2).

In sum, the above attempts to answer a simple question. If a company trades recklessly, to its own detriment and therefore to the detriment of its stakeholders, is the point of departure that an individual creditor may litigate against an errant director before the company has had an opportunity to do so first? The answer is equally simple — (1) the Act, literally, does not allow it; (2) a theoretical perspective on companies indicates it should not be the case; and (3) the doctrinal principles of juristic personality (as supported by case law) is in harmony with the theory — only in exceptional circumstances. Therefore, it cannot be the point of departure.

(b) Insolvent and in liquidation: the on-going operation of s 424

In spite of the fact that s 22(1) moves the remedial regime of company law onto a more sound doctrinal footing, s 424 (along with the rest of Chapter of XIV of the 1973 Companies Act) remains operative for companies that are insolvent and formally in liquidation; by virtue of s 79(1)*(b)* in conjunction with Schedule 5, Item 9.

Despite the fact that a liquidator takes over the management of a company in liquidation, and also constructively 'is' the body of creditors as the representative of their collective interests, s 424 remains operative. In effect, therefore, *once a company goes into formal winding up*, individual creditors are still able to claim directly from the company's directors (or 'any other person' responsible).[151]

V CONCLUSION

This article, through an analysis of the current Companies Act's remedies for directors' breach of the duty of care and skill, and a company's reckless trading, respectively, makes two main points. The first centres on the changing relationship between the two remedies, concluding that from the company's perspective there is little use for the former, as the latter presents a more viable course of action against errant managers.

In terms of the duty of care and skill, it makes two arguments. First, concerning negligence, it argues that although the negligence component of the care and skill inquiry has been made (if interpreted according to the heritage of provision's wording) more objective, and thus less

[151] If successful, the liquidators may be unable to recover losses on behalf of the company from these 'men of straw' once a s 424 judgment has been granted and executed.

forgiving of directors, the import of the business judgment rule has rendered this irrelevant. All that is currently required of directors who are reasonably informed is that their business judgments and resultant decisions bear a rational relationship to the reasons they were made. This rationality requirement allows directors to act so unreasonably that the only actionable level of unreasonableness is tantamount to gross negligence. Second, as a delictual action, the remedy has not only a very forgiving standard of conduct, but also contains the other four traditional elements of Aquilian liability, increasing the burden faced by a litigant-company attempting to utilise this historically toothless remedy. If it is argued that the common-law position requiring a subjective test to determine negligence has not been altered in this regard by the statutory duty, the business judgment rule *still* has the effect that the company must prove something very close to gross negligence to hold a director liable for breaching his duty of care and skill.

In this light, it analyses the remedy against directors for their acquiescence in the reckless trading of a company, which has under the new Act become available to the company itself as an alternative to breach of the duty of care and skill. It shows that — from case law as well as the interpretation of the Act — the remedy has far less onerous requirements. Most notable are (1) an essentially equivalent prescribed standard of conduct, which essentially comes down to gross negligence; as well as (2) a less complex set of elements activating liability, excluding both causation and wrongfulness. In conclusion, a company-plaintiff will most certainly opt for the latter remedy, which is not only less complex but also less onerous to pursue successfully.

The second broad point, in light of the conclusions of the first, is to what extent the contravention of the reckless trading provision provides a direct remedy for creditors against the directors who allowed the company to conduct its business in a reckless manner. This argument, focusing on both the structure of the current Act and the theoretical understanding of the firm that should underpin both it and certain elements of juristic personality, looks first at companies which are insolvent yet not in formal liquidation. In this context, it concludes that the Act may have effectively deprived individual creditors from utilising the remedy, doing so in favour of the company as the primary plaintiff. This conclusion is based on a hermeneutic analysis of the provisions of s 22(1), s 77(3)*(b)*, and s 218(2), which when read together may not necessarily form the basis of a cause of action for creditors wishing to hold directors personally liable for their complicity in the company's reckless conduct.

It further argues that this is — counter-intuitively — a step in the right direction. It is proposed that this serves the overall imperative of creditor protection much better than the old regime's provisions do, and uses a legal-economic policy analysis to justify such a more literal interpretation of these provisions of the Act.

Briefly, it derives its argument from the legal-economic theories of the firm and the function of juristic personality, as a standardised nexus of transaction- and agency-cost reducing contracts; but more importantly as a means with which to partition the assets of owners and managers from those of the firm itself to the benefit of creditors. If the legislature wanted to provide creditors with a direct remedy against *directors* for a breach of the reckless trading provisions, it is submitted that an appropriate amendment be made to s 218(2).

As the section currently reads, it is general in nature and not clear in terms of what is meant by 'contravenes any provision of this Act'. Furthermore, the point of departure of company law is limited liability and only where the legislature explicitly provides for personal liability should this point of departure be ignored.

It also argues that a narrower, more unforgiving interpretation of the Act does not deprive creditors of remedial recourse in exceptional circumstances. It shows creditors may still rely (1) on the statutory derivative action; and surprisingly (2) on breach of the duty of care and skill via s 218(2). Moreover, it shows that is the most efficient, effective and justifiable manner in which to construe the law. In this sense, the most surprising outcome of the overall analysis is that the roles of these 'remedies in flux' have to a limited degree reversed — the duty of care and skill serves individual creditors better than the company; the remedy against directors who allowed the company to trade recklessly serves the company better than individual creditors, which ultimately serves the overall body of creditors. Stranger still is the conclusion that this is for the best — whether an unintended consequence of the drafting of the 2008 Act, or an intentional and laudable realignment of policy objectives.

Lastly, in the context of companies already in winding up, it confirms that the provisions of the 1973 Act are in force, and that there is little to aid the concursus of creditors against a cleaning out of directors' coffers before they can be brought to task by the liquidator.