

Short notes on:

DIRECTORS' DELINQUENCY VERSUS PROBATION

Introduction

A significant innovation under the Companies Act 71 of 2008 as amended (the "Act") is that it provides for a court application to declare a director delinquent or to have him/her placed under an order of probation. The Act confers *locus standi* on a broad range of persons to apply to court for such an order and such applications can have far-reaching implications for directors. Also of significance is that a court may impose various restrictive conditions when granting such an order.

It is therefore crucial to unpack the relevant provisions.

The Act

In terms of section 162(5) of the Act, a court 'must' make an order declaring a person a delinquent director if he/she –

- *consented to serve as a director, or acted in the capacity of a director or prescribed officer, while ineligible or disqualified to be a director in terms of section 69 of the Act;*
- *while under an order of probation, acted as a director in a manner that contravened that order;*
- *while a director, grossly abused this position;*
- *while a director, contrary to section 76(2)(a) of the Act, took personal advantage of information or an opportunity, or intentionally or by gross negligence inflicted harm on the company or a subsidiary of the company;*
- *while a director, acted in a manner that amounted to gross negligence, wilful misconduct or breach of trust or in a manner contemplated in section 77(3)(a), (b) or (c) of the Act (unauthorised acts, reckless trading or fraud);*
- *has repeatedly been subject to a compliance notice or similar enforcement mechanism;*

- *has at least twice been personally convicted of an offence or subjected to an administrative fine or penalty in terms of any legislation; or*
- *within a period of five years, was a director of one or more companies or was a managing member of one or more close corporations, or controlled or participated in the control of a juristic person (irrespective of whether concurrently, sequentially or at unrelated times) that was convicted of an offence or subjected to an administrative fine or similar penalty in terms of any legislation.*

Conversely, a host of things are not sufficient for delinquency, these include poor decision-making, ordinary commercial misjudgement or a misguided reliance on incorrect professional advice.

Furthermore, because of use of the word 'must' in section 162(5), that court does not have the discretion whether to grant an order of delinquency if any of these grounds are established. In contrast, in terms of section 162(7) of the Act, a court 'may' declare a person under probation in the circumstances set out below and thus has a discretion whether to grant such an order.¹

The effect of an order being granted is that the director will be banned from being a director for at least seven years, or even for a lifetime in very serious cases. Moreover his/her name is put on a public register of disqualified directors. In addition, conditions may be imposed on a delinquency order, such as ordering the director to go for remedial education or to do community service.

Grounds of probation

In terms of section 162(7) of the Act, a court 'may' declare a person under probation if the person –

- *while a director, was present at a meeting and failed to vote against a resolution despite the inability of the company to satisfy the solvency and liquidity test, contrary to the Act;*
- *while a director, acted in a manner materially inconsistent with the duties of a director;*
- *while a director, acted in or supported a decision of the company to act in a manner that was oppressive or unfairly prejudicial in terms of section 163(1) of the Act; or*
- *within ten years after the effective date (1 May 2011) was a director of more than one company or a managing member of more than one close corporation (concurrently,*

¹ <http://www.saflii.org/za/journals/DEREBUS/2013/14.html>: accessed 12 September 2019

sequentially or at unrelated times), and during that time two or more of those companies or close corporations failed to fully pay all of their creditors or meet all their obligations (except under a business rescue plan resulting from a board resolution in terms of section 129 of the Act or a compromise with creditors in terms of section 155 of the Act).

Conclusion

It is important that directors, companies and stakeholders observe their duties with the necessary care and avoid delinquency. For affected companies, considering the remedy could be a crucial solution to a far-reaching problem. Contact SchoemanLaw for any of your corporate legal needs.

