The dissenting director

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EXECUTIVE SUMMARY

Healthy and robust debate and discussion between directors is an integral component of board functioning. The beginning point of deliberations may involve robust discussion and debate around the issue at hand. This may be reflected by differing views or disagreement on the matter.

The word “dissent” is used for the purposes of this paper to describe the situation after these two stages have passed and the director cannot reconcile himself to the direction taken by the board as a whole. It is at the stage when disagreement turns to dissent that a director needs to carefully consider his position and the available options.

Issues such as the strategic path that the company takes into the future are more likely than others to result in disagreement. We set out guidelines and considerations for the director when faced with these issues in our sections on “Sensitive issues that may provoke dissent” and “Guidelines for dissenting directors”.

Companies with boards that do not entertain disagreement nor engage with management, or challenge their decisions, need to consider whether the board culture is conducive to healthy debate. They also need to consider whether directors with the appropriate levels of expertise and experience have been appointed.

The role of the chairman is also a pivotal one in this area. We discuss this in more detail in our sections dealing with “Possible reasons for an absence of healthy debate” and “The role of the chairman”.

1. Introduction

The concept of an effectively functioning board is one that brings to mind optimal decision making in an atmosphere of mutual respect, trust, candour and open debate. However, it is to be expected that within
This atmosphere, disagreements, differences of view, and in some instances, dissent will arise.

This paper seeks to highlight the importance of raising the dissenting voice. It also provides practical guidelines for doing so in the best interests of the various stakeholders.

The board of directors collectively (and those individuals that constitute it) is charged with making decisions on behalf of the company. Directors’ duties arise from the common law, the Companies Act and other legislation. The company’s articles of association may impose further duties upon its directors.

A director acts in a ‘fiduciary’ capacity in relation to the company. This fiduciary duty entails that directors at all times act honestly and in the best interest of the company. Displaying dissent when required, and acting with unfettered discretion, forms part and parcel of this primary fiduciary duty. The director therefore has a responsibility to make his voice heard where he disagrees with a certain course of action.

2. The essence of dissent

The terms “disagreement” and “dissent” as used in the paper are not meant to be synonymous. As illustrated below, disagreement does not necessarily constitute dissent but may lead to dissent.

Before directors can be in a position to decide on a proposal put before the board, it is essential that they have a proper grasp of the facts and assumptions that underpin it. The first step when differences of opinion arise therefore is for directors to understand these facts and assumptions. Initial differences of opinion may arise over the underlying facts and assumptions and these need to be clarified at the outset in order to ensure that the debate is conducted from the correct premise.

More serious disagreement may arise over the purpose or objectives sought to be achieved by a proposed course of action. Such proposals should be consistent with the strategic direction of the company, which should already have been agreed upon by the board.

Another possible cause of disagreement may be the method of implementation. This will often arise from differences in the perceived risks inherent in the proposed approach, as compared to alternative options. Disent on matters of ethics or principle are the most difficult to deal with. Personal and religious convictions aside, there are various other ethical considerations, such as fairness and transparency that come into play when business transactions are concluded and the board must consider these.

Disagreement on fundamental issues such as fraudulent, reckless, grossly negligent or unlawful conduct is most likely to lead to formal dissent. It is important that the board debate should be conducted in such a way that the focus is on the issues involved and effect that they will have on the long-term benefit of the company.

The extent of disagreement may vary from a minor difference of opinion over an immaterial issue to a fundamental disagreement. The latter, if it is unresolved, may result in the formal dissent from a board decision by one or more directors.
3. Characteristics of constructive dissent
Dissent is not the same as disloyalty but rather an honest expression of a director’s responsibility to act in the best interest of the company. The knowledge by each director that other members of the board take their responsibilities seriously, creates a stronger, more effective monitoring unit.

Enterprise involves risk taking in order to achieve its objectives. Effective decision making entails understanding these risks and assessing whether the company is managing the risks appropriately. Dissent is inappropriate if aimed at avoiding risk in its totality. Dissent should therefore not be used to stifle innovation and business initiative. It is the final expression of a director’s personal opinion in the process of exercising his or her fiduciary duty.

4. Sensitive issues that may provoke dissent
Dissent may arise in relation to major decisions that may include:
• formulation of strategy;
• implementation of strategy;
• dividend policy;
• unlawful conduct;
• appointment, retention, retirement and re-appointment of directors; and
• issues relating to company culture, ethics and value systems.

5. Formalities of dissent
Board decisions are taken collectively and it is assumed that each director was party to a decision, unless indicated otherwise. Directors who disagree with a decision may be deemed to have consented unless they formally dissent. In most jurisdictions abstaining from voting does not constitute dissent.

It is therefore important that corporate minutes preserve an accurate and official record of the proceedings of a board or committee meeting. Well-kept corporate minutes and directors resolutions serve as a record of corporate decisions and reflect director dissent where appropriate.

6. Guidelines for dissenting directors
Where a director is in disagreement with a board decision, the following guidelines are available to the director:

• The director should raise his or her concerns at the board meeting and obtain all information necessary to make the decision.

• If still in disagreement, the director should thereafter engage in robust debate at the meeting and put forward facts and arguments in favour of his or her view.

• In raising a dissenting voice, the director should always ensure that he or she is doing so on an informed basis. To this end the use of an independent professional may be required.

King II states that directors “must, if in doubt about any aspect of their duties, obtain independent professional advice at the earliest opportunity”. King II also requires that the “board should have an agreed procedure whereby directors may,
if necessary, take independent professional advice at the company’s expense.”

- Upon having obtained this advice, the director should arrange for further board discussion relating to the matter.

- If, after receipt of further information and the additional board discussion the director is still dissatisfied, he or she may request the formal recording of the dissenting view in the resolution of the meeting where the matter is discussed.

- For concerns arising between scheduled meetings, the director can approach the chairman or company secretary in order to convene a special meeting.

- The above may include drafting and distributing a detailed memorandum of concerns to the other directors and to request discussion of this memorandum at the special meeting. If the chairman is not willing to convene a special meeting to discuss the issue, the articles of the company should be consulted to determine if an individual director has the power to call a meeting.

- Having taken the steps above, if the view of the dissenting director is then voted against or overruled on a matter which he or she regards as one of fundamental principle, and he or she is of the opinion that serious harm to the company is likely to result, the director may have no option but to resign from the board.

- A director intending to resign should obtain legal counsel on his or her course of action.

- At this stage the director should consider issuing a statement to the board explaining his or her position together with his or her resignation. In this instance the director should seek legal counsel to ensure fiduciary duties and responsibilities are not breached.

- The director should discuss and preferably agree with the board the nature of the public communication regarding the resignation bearing in mind the fine line between the duty of confidentiality to the company and the duty to report to shareholders in an open and transparent manner so as to enable them to properly exercise their powers of appointing directors.

- If the matter is one that will be reported to shareholders in a circular or annual report, the chairman may allow the director the right to require that it be recorded in the circular or annual report that the decision of the board was not unanimous.
A director is bound by the fiduciary duty to maintain confidentiality with respect to information acquired about the company’s operations and affairs in his or her capacity as director, as well as any provisions contained in his or her service contract. This duty continues after the director has left the board. It is only in rare circumstances that the duty to maintain confidentiality is overridden by the duty to report to other authorities, for example a requirement to report corruption under the relevant statutes. Where there is a legal obligation on the director to report, this would not result in a breach of fiduciary duty. In all instances the director would be advised to seek legal counsel before disclosure.

7. Possible reasons for an absence of healthy debate
A board culture which discourages robust debate is one of the possible reasons for a lack of director involvement. Other reasons may be:
- The view that directors should be completely loyal to the chairman and support management demands creates a culture of conformity and dampens or eliminates healthy discussion and debate.
- Shortcomings in the selection process and the training of new directors may result in boards being over-weighted with inexperienced members incapable of dealing with complex corporate issues.
- The chairman may not understand how to manage the board deliberation process or lack the necessary skills to do so.
- Directors may lack the expertise, confidence and courage to analyse the company’s problems and opportunities.
- Directors may not be groomed in board etiquette and may therefore be of the view that to ask a question in a board meeting is inappropriate.
- Directors do not adequately prepare for complex issues discussed at board meetings.

8. The role of the chairman
The chairman of the board is primarily responsible for the effective functioning of the board. This includes inter alia to preside over meetings of directors and to ensure the smooth operation of the board. The chairman therefore has the key role in managing debate, disagreement and ultimately dissent.

It is the duty of the chairman to encourage healthy and robust debate over decisions and ultimately strike the correct balance between too little and too much debate.

9. Conclusion
The role of critical and robust debate, disagreement and dissent at the appropriate levels and in the appropriate manner is undeniable in shaping the future of a company and maximising value. To this end, directors must act with courage in the face of possible reprisals and stand firm in their conviction to do that which is
in the best interests of the company. This is required not only as it is a legal responsibility of directors but more importantly because ethical standards demand it.

10. References

- Companies Act 61 of 1973, South Africa.
- King Report on Corporate Governance for South Africa, 2002
# GUIDELINE FOR DISSENTING DIRECTORS

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<thead>
<tr>
<th>Options</th>
<th>Step 1:</th>
<th>Step 2:</th>
<th>Step 3a:</th>
<th>Step 3b:</th>
<th>Step 4a:</th>
<th>Step 4b:</th>
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<td>• Obtain all information necessary to make decision. • Engage in robust debate at meeting and put forward facts and arguments in favour of your view.</td>
<td>Obtain independent professional advice and arrange for further board discussion.</td>
<td>Despite initial views, based on further facts and debate, agree to support decision.</td>
<td>If still do not support decision, request formal recording of dissenting view in resolution.</td>
<td>Consider appropriate further steps and obtain professional advice in this regard. Resignation and possible notice/communiqué to shareholders/other parties. Must still be acting in the interest of the company.</td>
<td>Consider appropriate further steps and obtain professional advice in this regard. Report to the relevant authorities where required by law.</td>
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**Dissent on a matter of business judgement eg. strategy.**

| Obligatory | Optional depending on the importance of the issue. | No action | Recommended | Optional depending on the importance of the issue. | Not applicable |

**Dissent on matter of perceived business ethics or principle.**

| Obligatory | Recommended | No action | Obligatory | Recommended subject to legal advice, and provided ethical issue is in relation to company and not personal view (for example on smoking, gambling, etc)*. | Not applicable |

**Dissent on fundamental matter that may constitute fraudulent, reckless, grossly negligent or unlawful conduct.**

| Obligatory | Obligatory | Where a fundamental matter is concerned, action is necessary. | Obligatory | Obligatory subject to legal advice. | Obligatory |

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* Where the personal values and ethics of a director conflict with the business of the company but are not generally offensive to the values of that company (for example a company has an investment in a casino but a director is religious and does not support gambling), this kind of personal conflict does not require the actions set out above. The director should consider resignation if his/her fundamental values and ethics are not reconcilable with the business model of the company.