IoDSA FAQs
The Business Judgment Rule
Frequently Asked Questions

The Business Judgment Rule

1. What are the important factors to consider by a director in performing his duties?

S76 (3) of the Companies Act No. 71 of 2008 states that directors must perform their duties

(a) in good faith and for a proper purpose;  
(b) in the best interests of the company; and  
(c) with the degree of care, skill and diligence that may reasonably be expected of a person carrying out the same functions in relation to the company as those carried out by that director; and having the general knowledge, skill and experience of that director.

This test is applied differently to different types of directors. The extent of a director’s duty of care and skill depends on the nature of the company’s business, that our law does not require a director to have special business acumen, and that directors may assume that officials will perform their duties honestly.

2. How will a director know when he has carried out his responsibilities appropriately?

S76 (4) states that a director is considered to have satisfied the obligations of acting in the best interests of the company; and with the degree of care, skill and diligence that may reasonably be expected of a person carrying out the same functions in relation to the company as those carried out by that director; and having the general knowledge, skill and experience of that director if the director has:

1. taken reasonably diligent steps to become informed about the matter;
2. either—
   (aa) the director had no material personal financial interest in the subject matter of the decision, and had no reasonable basis to know that any related person had a personal financial interest in the matter; or
   (bb) the director complied with the requirements of section 75 with respect to any interest contemplated in subparagraph (aa); and
3. the director made a decision, or supported a 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

This is the essence of the ‘business judgement rule’ which entered the South African legal lexicon with the arrival of the Act.

3. What does this mean for directors?

Business is about taking risk for reward. In doing so, directors, whether executive or non-executive, are required to exercise their judgement as to the best decisions or courses of action available to a company. However, sometimes even the best laid plans fail, and, in such instances, the assessment of the appropriateness of the decisions taken by the directors is not based solely on the manner in which the decision turned out, but is also based on the process that the directors followed in arriving at their decision.

The ‘business judgement rule’ has been heralded by many as the key form of protection for directors, and allows them to make informed judgements without the threat of liability hanging over their heads and seeks to protect directors from liability to the company and shareholders as a result of poor decision-making. The rule contained within South African law is considered to be broader than the equivalent rule in other countries, as it is not limited to judgements made by the directors but instead applies to all decisions that a director may take as it relates to the performance of his or her powers and functions.

It is critical to note that the ‘business judgement rule’ can only be utilised if all of the requirements discussed above, as set out in the Act, have been complied with. Additionally, the Director, Prescribed Officer or Committee Member must have been acting in furtherance of a lawful and legitimate corporate purpose.

For further information on this topic, including guidance on each of the elements of the definition and some practical considerations, view the Corporate Governance Network’s position paper on the IoDSA website https://c.ymcdn.com/sites/iodsa.site-ym.com/resource/collection/05E93ACB-10BE-4507-9601-307A66F34BD8/IoD_Business_JudgementEmail.pdf