



**SCHOOL OF GRADUATE STUDIES  
COLLEGE OF LAW AND GOVERNANCE  
SCHOOL OF LAW (LLM CLASS, COMMERCIAL LAW PROGRAM)**

**SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE  
MASTER OF LAWS DEGREE AT THE SCHOOL OF LAW, HAWASSA UNIVERSITY  
TITLE: DUTIES AND LIABILITIES OF SHARE COMPANY DIRECTORS UNDER  
THE NEW COMMERCIAL CODE OF ETHIOPIA: LESSONS FROM SOME  
SELECTED COUNTRIES.**

**BY: JEMIL KEDIR**

**ADVISOR: ANDUALEM NEGA (ASST. PRO)**

**MAY, 2024  
HAWASSA, ETHIOPIA**

**HAWASSA UNIVERSITY**

**DUTIES AND LIABILITIES OF SHARE COMPANY DIRECTORS UNDER THE NEW  
COMMERCIAL CODE OF ETHIOPIA: LESSONS FROM SOME SELECTED  
COUNTRIES.**

**BY: JEMIL KEDIR GELGELU**

**ADVISOR: ANDUALEM NEGA (ASST. PRO)**

**SUBMITTED IN PARTIAL FULFILLMENT OF THE  
REQUIREMENTS FOR THE MASTER OF LAWS DEGREE AT THE SCHOOL OF  
LAW, HAWASSA UNIVERSITY**

**MAY, 2024  
HAWASSA, ETHIOPIA**

## DECLARATION

I hereby declare that “**DUTIES AND LIABILITIES OF SHARE COMPANY DIRECTORS UNDER THE NEW COMMERCIAL CODE OF ETHIOPIA: LESSONS FROM SOME SELECTED COUNTRIES.**” is my original work, that has not been submitted for a degree at any other university, and that all sources of material used for this thesis have been properly acknowledged.

\_\_\_\_\_

Name

\_\_\_\_\_

Date

\_\_\_\_\_

Signature

## APPROVAL SHEET

This is to certify that the thesis entitled “**DUTIES AND LIABILITIES OF SHARE COMPANY DIRECTORS UNDER THE NEW COMMERCIAL CODE OF ETHIOPIA: LESSONS FROM SOME SELECTED COUNTRIES.**” submitted in partial fulfillment of the requirements for the degree of Master's with specialization in commercial law, the Graduate Program of the School of law, and has been carried out by **JEMIL KEDIR GELGELU** ID. No. GPCLW/OO07/14 under my supervision. Therefore I recommend that the student has fulfilled the requirements and hence hereby can submit the thesis to the department.

---

Name of advisor

---

Signature

---

Date

**EXAMINER'S APPROVAL SHEET**  
**SCHOOL OF GRADUATE STUDIES**  
**HAWASSA UNIVERSITY EXAMINERS' APPROVAL SHEET**

We, the undersigned, members of the Board of Examiners of the final open defense by **Jemil Kedir** have read and evaluated his/her thesis entitled “ **DUETS AND LIABILITY'S OF SHARE COMPANY DIRECTORS UNDER THE NEW COMMERCIAL CODE OF ETHIOPIA: LESSON FROM SOME SELECTED COUNTRIES** ” and examined the candidate. This is, therefore, to certify that the thesis has been accepted in partial fulfillment of the requirements for the degree.

_____	_____	_____
Name of major advisor	Signature	Date
_____	_____	_____
Name of Internal examiner-I	Signature	Date
_____	_____	_____
Name of Internal examiner-II	Signature	Date
_____	_____	_____
Name of External examiner	Signature	Date
_____	_____	_____
SGS Approval	Signature	Date

Final approval and acceptance of the thesis is contingent upon the submission of the final copy of the thesis to the school of graduate studies (SGS) through the department/ school graduate committee (DGC/SGS) of the candidates department.

Stamp of SGS

Date: \_\_\_\_\_

## **Acknowledgement**

First of all, I would like to thank the Almighty Allah for His mercy and protection in my academic journey!!!

My special thanks go to my supervisor Andualem Nega (Assistant professor) for his invaluable guidance and support throughout the research process. His expertise and humble approach helped me to accomplish this research.

I am deeply thankful to my beloved wife Rukia Muhammed and my family for their love and support during this process. Without their encouragement and motivation, I would not have been able to accomplish this tedious academic journey. I am also grateful to my brother Abdulfeta Abdurahman for his encouragement and support in this journey.

## **Abstract**

*This research examines the duties and liabilities of share company directors under the new Ethiopian commercial code, comparing it with South African, United Kingdom, and German company law. The study aims to examine the best experiences and lessons learned from these countries and draw lessons for the Ethiopian system. The research highlights the limitations of the revised Ethiopian commercial code, recommending that directors must operate in the best interests of shareholders. However, the director's duty of loyalty did not include all three components: refraining from using corporate opportunities for personal gain, refraining from having a personal stake in business transactions with third parties, and maintaining confidentiality of corporate information. Despite these shortcomings, the new Ethiopian commercial code remains effective compared to foreign jurisdictions. The research also provides recommendations for improving the Ethiopian commercial code.*

**Keywords: Corporate governance, Commercial Code, Share Company, Duties and Liabilities of Directors, Ethiopia.**

## **ABBREVIATIONS AND ACRONYM**

**FDRE:** Federal Democratic Republic of Ethiopia

**UK:** United Kingdom

**AktG :** Aktiengesetz

**HGB:** Handelsgesetzbucz

**BGB:** Bürgerliches Gesetzbuch

## Contents

Acknowledgement .....	i
Abstract .....	ii
ABBREVIATIONS AND ACRONYM .....	<b>Error! Bookmark not defined.</b>
Chapter One .....	1
Background of the Study .....	1
1.1 Introduction.....	1
1.2 Statement of the Problem.....	3
1.3 Research Questions .....	5
1.4 Objectives of the Study.....	5
1.5 Literature Review.....	6
1.6 Methodology .....	9
1.7 Scope of the Research.....	9
1.8 Limitations of the Study.....	9
1.9 Significance of the study.....	10
1.10 Structure of the study .....	10
Chapter Two.....	11
Duties and Liabilities of Directors under Ethiopian Law .....	11
2.1 Introductions.....	11
2.2 Corporate Governance in General.....	11
2.3 The Nature of Corporate Governance .....	13
2.4 Theories of Corporate Governance .....	13
2.4.1 Agency Theory.....	14
2.4.2 Stockholder/shareholder Theory .....	15
2.4.3 Theories of Convergence .....	16

2.4.4 Stakeholder Theory .....	16
2.4.5 Stewardship Theory .....	17
2.5 Corporate Governance and the Board of Directors .....	19
2.6 Duties and Liabilities of Directors under the Ethiopian Corporate Governance Code ..	20
2.6.1 Duties of Directors under the Ethiopian Corporate Governance Code.....	21
2.6.2. Liabilities of Directors under the Ethiopian Corporate Governance Code.....	25
2.7 Conclusion.....	27
Chapter Three.....	28
Duties and Liabilities of Directors under the Foreign Jurisdictions .....	28
3.1. Introduction.....	28
3.2 The South African Company Law: An Overview .....	28
3.2.1 The South African Companies Act 71 of 2008.....	29
3.3. The Director's Duties and Liabilities under the Existing South African 2008 Company Act .....	31
3.3.1 Duties of directors under the 2008 company Act .....	32
3.3.2 Liability of directors under the 2008 company Act .....	36
3.4 The United Kingdom Company Law: An Overview .....	39
3.4.1 The UK Companies Act 2006.....	40
3.4. The Director's Duties and Liabilities under the existing UK 2006 Company Act .....	41
3.4.1 Duties of directors under the 2006 company Act .....	41
3.4.2 Liability of directors under the 2006 UK Company Act .....	43
3.5 The German Company Law: An Overview .....	45
3.5.1 The German Corporate Governance of Stock Corporations.....	46
3.5.2 The Director's Duties and Liabilities under the existing Germany Company law .....	47
3.5.3 The Duties of directors under Germany Company Law .....	48
3.5.4 Liability of directors under the German Stock Corporation Act .....	50
3.6 Conclusion .....	53
Chapter Four .....	54
Directors' Duties and Liabilities under the Ethiopian Company Law: Lessons from South African, UK and Germany Company Law .....	54
4.1 Introduction.....	54

4.2 The formulation of directors' Duties and Liabilities under the revised Ethiopian Company Law: Lessons from South African UK and German Company Law .....	54
4.2.1 Significant changes brought by the revised commercial code.....	54
4.2.2. Directors' Duties under the new Ethiopian commercial law and Lessons from South African Company Law.....	55
4.3 Directors' liabilities under the new Ethiopian commercial law and Lessons from South African, United Kingdom and German Company Law .....	61
4.4 Conclusions.....	64
4.5 Recommendations.....	67
Bibliography .....	69

# Chapter One

## Background of the Study

### 1.1 Introduction

Running businesses is crucial for a country's development and the economic well-being of its citizens.<sup>1</sup> To achieve economic success, the legal system must be supportive, flexible, and well-regulated. Emperor Haile Selassie of Ethiopia proposed the introduction of the Commercial Code of the Empire of Ethiopia in 1960, which was issued nearly sixty years ago.<sup>2</sup>

The 1960 Commercial Code of the Empire of Ethiopia,<sup>3</sup> (the Commercial Code), has been the basis of many modern laws in the country. Nevertheless, on March 25, 2021, the Ethiopian House of People's Representatives approved a new version of the country's Commercial code. The new commercial code has introduced various changes and new concepts that did not exist in the previous commercial code.<sup>4</sup> Under the old commercial code, only six options were available for setting up a business organization in the country. These included ordinary partnerships, joint ventures, general partnerships, limited partnerships, share companies, and private limited companies.<sup>5</sup>

The existing commercial legislation has altered this by modifying limited liability partnerships and one-person private limited companies while removing ordinary partnerships from the list.<sup>6</sup> A trader can now change his company's legal status from a sole proprietorship to a one-person PLC. However, any debts accrued before the conversion that led to the formation of the one-person PLC will still be subject to the trader's joint and severally liable to the company.<sup>7</sup> A limited liability partnership is a business arrangement where partners are only held responsible for the amount they have invested in the company.<sup>8</sup> So, in the event of a partnership failure, the partners' private assets or income are immune from creditors' claims.

---

<sup>1</sup>Commercial Code of Ethiopia preface, Proclamation No. 1243/2021.

<sup>2</sup>Ibid

<sup>3</sup> Commercial Code of Ethiopia, *Negarit Gazeta, Extraordinary issue*, proclamation no.3 (1960).

<sup>4</sup> Ashenafi Endale, 'A Bird's Eye View of the Revised Commercial Code'(2022) Ethiopian Business Review <<https://ethiopianbusinessreview.net/a-birds-eye-view-of-the-revised-commercial-code/>> accessed in 24 sep 2023

<sup>5</sup>Article212 of the Commercial Code.

<sup>6</sup> Commercial Code of Ethiopia 2021 arts 172–174.

<sup>7</sup> Ibid arts 221–233.

<sup>8</sup> Ibid art. 221.

The form of business organizations named as companies under the new Commercial Code are three types: Share Companies,<sup>9</sup> Private Limited Companies,<sup>10</sup> and one-person private limited companies.<sup>11</sup>

Even though numerous significant changes were made, the new commercial code did not replace the previous one.<sup>12</sup> Splitting previous codes into commercial and financial services codes is the most significant change.<sup>13</sup> Despite being announced 60 years ago and including company law, the old Commercial Code has not yet been thoroughly tested and evolved in practice.<sup>14</sup> Even though the Commercial Code of Ethiopia from the 1960s contains provisions relevant to the corporate governance of share companies, it is claimed that these provisions lack the comprehensiveness and clarity needed to address them.<sup>15</sup>

Current issues in corporate governance to the board of directors include their responsibilities, composition, independence, special board committees, audit, remuneration and nomination committees, separation of roles of chairman and CEO, and procedures for deterring conflicts of interest.<sup>16</sup> It was anticipated that the new Commercial Code would alleviate these issues by considering other nations' experiences. Besides the practical implementation of the law related to share companies and corporate governance are of utmost importance for the country.

Different countries use different frameworks to control company governance. And many theories define and explain the term corporate governance Corporate governance structures help reduce the transaction costs associated with the specialization of organizational functions by serving as a collection of institutional arrangements that tend to align the interests of management and shareholders who bear risk.<sup>17</sup> However, several countries are commonly recognized for having

---

<sup>9</sup> Ibid arts 245–494.

<sup>10</sup> Ibid arts 495–533.

<sup>11</sup> Ibid arts 534–545

<sup>12</sup> Fekadu Petros, 'The New Ethiopian Commercial Code: A Highlight of Major Changes'(2022) Fekadu Petros & Partner Law Office< <https://fekaduandpartners.com/download/the-new-ethiopian-commercial-code-a-highlight-of-major-changes.pdf>> accessed in 5 September 2023

<sup>13</sup> Ibid

<sup>14</sup> Addis Ababa Chamber of Commerce, *Position of the Business Community on the Revision of the Commercial Code of Ethiopia* (2008) 7.

<sup>15</sup> Hussein Ahmed Tura, 'Corporate Governance In Ethiopian Share Companies: What Should The Future Look Like?'( A Master's Thesis Submitted to School of Graduate Studies of Addis Ababa University in Partial Fulfillment of the Requirements of Masters of Law (LL.M),2011) 3.

<sup>16</sup> Fekadu Petros, 'The New Ethiopian Commercial Code: A Highlight of Major Changes'(2022) Fekadu Petros & Partner Law Office< <https://fekaduandpartners.com/download/the-new-ethiopian-commercial-code-a-highlight-of-major-changes.pdf>

<sup>17</sup> Barry D Baysinger, and Butler N Henry, 'Corporate governance and the board of directors: Performance effects of changes in board composition' (2019) *Corporate Governance*. Gower., 215-238

strong corporate governance frameworks and regulations that outline the duties and liabilities of company directors. The selected countries' business—England, Germany, and South Africa, which has a long history and is used widely, is well-developed, and many African nations utilize it as a guide.

Thus, learning from the company laws and implementations of selected countries will be beneficial, particularly in how directors' obligations and liabilities are managed in light of the potential gaps in Ethiopian company law. This thesis discusses the corporate governance of companies in law and practice, the responsibilities and liabilities of directors, the legal and practical framework of other countries' company law concerning company directors, and attempts to draw lessons from the vast experience of those countries. Finally, it will also make recommendations.

## **1.2 Statement of the Problem**

A company is a juristic person. When a company acts, it does so through its board of directors.<sup>18</sup> Most of the time, a director's obligations are linked to their authority and liabilities. They are stated to have three different responsibilities, namely loyalty, diligence, and obedience.<sup>19</sup> Directors have been alternatively viewed as trustees, agents, managers, and caretakers of the company they serve.<sup>20</sup> Whatever the view has taken, a director occupies a position of trust with the company.<sup>21</sup>

Although Article 296 of the new Commercial Code does not define a director, it does include a concise description of the composition of the board of directors unlike the repealed Commercial Code that did not. The lack of definition of what a director means in the new commercial law also creates problems. However, according to Banking Business Proclamation No. 592/2008, a director is "any member of a bank's board of directors, regardless of his title."<sup>22</sup> Accordingly, it is crucial to consider the nature of the position and its responsibilities to decide whether a person qualifies as a director or not.

---

<<http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.962.1155&rep=rep1&type=pdf>> accessed in 7 august 2023

<sup>18</sup>Section 66 (1) of the Companies Act 71 of 2008.

<sup>19</sup> Harry C. Henn, *Laws of Corporation* (New York, West Group 1983) 3rd ed P. 612

<sup>20</sup>Ibid

<sup>21</sup>Cassim FHI, Cassim M.F., Cassim R, Jooste R, Shev J, and Yeats J, *Contemporary Company Law*, 2nd edn (Juta and Company, Claremont 2012) 412.

<sup>22</sup> Banking Business Proclamation, 2008, Proclamation No. 592, Federal Neg. Gaz. Year 14, No 57

According to the old Commercial Code of Ethiopia Article 347(1), the board of directors is the ultimate managing body of the company. It enjoys extensive powers as provided in the code and under the Memorandum and Articles of Association. In practice, the responsibility of management is given to the CEO (general manager), who in turn may delegate the responsibility to other senior executives.<sup>23</sup> Therefore, the board occupies a critical position between the shareholders (owners) and the company management.<sup>24</sup>

Articles 347 through 367 of the commercial codes, which were repealed, cover the twenty-one requirements that govern the board of directors. These regulations address a variety of subjects, including the protection of minority shareholders and the appointment, compensation, firing duties, and liabilities of the board of directors. However, the Ethiopian company law lacked sufficient legislative provisions on governance issues of the division of supervision and management responsibilities, as well as on the composition, independence, and compensation of the board of directors, as experts and businesses realized over time<sup>25</sup>

Article 325 of the new commercial law clearly states directors' obligations to the company. In light of this, directors are jointly and severally accountable to the firm for losses brought on by their negligence.<sup>26</sup> As a result, the business may assert any or all of them and recover the full number of damages from any or all of them. The law lacks an objective standard of culpability in this regard<sup>27</sup>

The directors' appointment, mandate, duties, and liabilities enshrined in the revised Commercial Code of Ethiopia lack clarity and coherence. There is also a gap in the law, like its scope of application for prescribed officers, board members, and shadow directors. Therefore, examining the scope of the director's duties and liabilities, gaps, and deficiencies and taking lessons from well-developed some selected countries' company law is worthy of research.

Directors' duties and liabilities are becoming popular in Ethiopian legal literature, although often missing empirical research.<sup>28</sup> In Ethiopia, the number of companies formed or under the process

---

<sup>23</sup> Tura (n 32) 57.

<sup>24</sup> Ibid

<sup>25</sup> Misganaw Belete, THE NEW ETHIOPIAN COMMERCIAL CODE: UNCOVERING THE MAJOR CHANGES IN COMPOSITION, ROLE, AND ACCOUNTABILITY OF THE BOARD OF DIRECTORS( 2022) Commercial Law Blog < <https://www.abysinialaw.com/blog-posts/itemlist/user/9359-misganawbelete>> accessed in 8 feb 2023

<sup>26</sup> Article 325 of The FDRE Commercial Code

<sup>27</sup> Belete (n 46)

<sup>28</sup> Minga Negash, 'Rethinking Corporate Governance in Ethiopia'<sup>2</sup>, KefeneGurum, 'Powers and Liabilities of Directors under the Commercial Code of Ethiopia' 72, Mekonnen Shiferaw, 'Rights, Duties and responsibilities of Directors in Financial Sector in Ethiopia' 10.

of formation with thousands of shareholders is increasing.<sup>29</sup> In this widespread situation, many corporate governance issues are emerging concerning companies.<sup>30</sup>

Although the Commercial Code of Ethiopia incorporates provisions pertinent to the corporate governance of companies, such provisions are said to lack comprehensiveness and clarity in addressing contemporary issues in corporate governance, specifically those related to liabilities and duties of directors.<sup>31</sup> That is to say, the legal framework governing the duties and liabilities of directors does not sufficiently address the issues related to the topic. Besides, the relevant law provisions, among others, do not delineate between corporate management and corporate governance.<sup>32</sup> Moreover, the law does not address the issue based on international experiences.<sup>33</sup> Therefore, it is imperative to address the shared company directors' related problems in the Commercial Code to devise solutions for the future since the number of companies is increasing in the country.

### **1.3 Research Questions**

This study examined the following research questions:

1. What are directors' duties and liabilities under Ethiopian share company law?
2. How are Share Company directors regulated under the law of some selected countries in practice?
3. What lessons can be drawn from those countries' share company law for reforming Ethiopian share company law, particularly regarding directors' duties and liabilities?

### **1.4 Objectives of the Study**

#### **1.4.1. General Objectives of the Study**

The study has the following objectives,

---

<sup>29</sup>Ethiopian Ministry of Trade Archive, Addis Ababa Ethiopia.

<sup>30</sup>Some of these are: the definition of directors, how a juristic person assumes directorship, scope of authority of directors etc. These are, *inter alia*, the research questions to be addressed by this dissertation.

<sup>31</sup>Sections 296,306,315,318,320 of the Revised Commercial Code of Ethiopia.

<sup>32</sup>Section 1 ch 4 of the Revised Commercial Code of Ethiopia.

<sup>33</sup>The Revised Commercial Code disregards the experience of other countries like South Africa which prohibits juristic persons from assuming directorship. This law also does not define what a director is. The issue of shadow directors is not addressed in Ethiopian law while it is addressed in UK Company Law.

- To examine the directors' duties and liabilities under the Ethiopian share company law.
  1. To assess whether and if the new Commercial Proclamation No. 1243/2021 addresses the duties and liabilities of directors in congruence with the purpose of revised company law.
  2. To examine how Share Company directors are regulated under the law of some selected countries in practice.
  3. To enshrine lessons drawn from those countries' share company law for reforming Ethiopian share company law, particularly regarding directors' duties and liabilities.

### 1.5 Literature Review

The corporate governance debate is worthy, given the connection between corporate governance and the financial performance of companies.<sup>34</sup> There are many corporate governance mechanisms,<sup>35</sup> some are market-based, while others have a significant role in the law. In the latter category is a range of duties owed by share company directors.<sup>36</sup>

A director's duties are generally seen as an important corporate governance mechanism.<sup>37</sup> These duties address conflicts between shareholders and directors by focusing upon the possibility of shirking by directors (addressed by the duty of care, skill, and diligence) and the possibility of lack of loyalty by directors (addressed by the duty to act honestly and in the best interest of the company).<sup>38</sup>

In South Africa, before the Act's enactment, directors' duties were derived mainly from the Common Law principles, case law, and certain provisions of the Companies Act of 1973. Under common law, directors had fiduciary duties to act in good faith, in the best interests of the company, and with the required skill and care. These duties were based on the general principles of company law and the directors' position as agents of the company.<sup>39</sup> The Act has resulted in the partial codification of directors' duties.<sup>40</sup>

---

<sup>34</sup> Ian M Ramsay (ed), *Corporate Governance and the Duties of Company Directors* 13.

<sup>35</sup> *Ibid* 13.

<sup>36</sup> *Ibid*

<sup>37</sup> *Ibid* 10.

<sup>38</sup> *Ibid*

<sup>39</sup> Cassim (n 31) 509.

<sup>40</sup> The Companies Act, No 71 of 2008, An Explanatory Guide (dti) 32.

Several other duties flow from this duty, such as the duty to avoid a conflict of interests.<sup>41</sup> A director's duty not to appropriate a corporate opportunity belonging to the company of which he or she is a director also flows from the duty to avoid a conflict of interests.<sup>42</sup>

In South Africa, the Act partially codified the duties of directors.<sup>43</sup> A director is obligated to perform significant fiduciary obligations under the Act and common law as of the time of their appointment.<sup>44</sup> Regarding directors' liability, the Act makes it explicit that, unless otherwise provided by the Act or the company's memorandum of incorporation, a person is not liable for any liabilities or obligations of a company simply by being an incorporator, shareholder, or director of a company.<sup>45</sup> Only certain circumstances allow for liability against a company's directors.<sup>46</sup> The director of a company may be held accountable under the Act for any loss, damages, or expenses incurred by the share company as a result of the director's violation of a duty outlined in the standard of directors' conduct, failure to disclose a personal financial interest in a particular matter or violation of an Act provision or the company's memorandum of incorporation.<sup>47</sup> In the United Kingdom, before the enactment of the Companies Act 2006, directors' duties were derived from a combination of common law principles, equitable principles, and various statutes. The common law and equitable principles formed the foundation of directors' duties, while statutes added specific requirements and regulations.

In Germany, before the enactment of specific statutes governing directors' duties, directors' duties were primarily derived from legal principles established by case law, as well as provisions of the German Civil Code (Bürgerliches Gesetzbuch, BGB) and the German Stock Corporation Act (Aktengesetz, AktG).<sup>48</sup>

Under German law, directors owe fiduciary duties to the company (Aktiengesellschaft, AG) and its shareholders. These duties are derived from general principles of civil law and corporate law. The primary legal principles governing directors' duties in Germany include Duty of Care, Duty of Loyalty, and Business Judgment Rule. The German Civil Code (BGB) provides general principles of civil law that apply to directors' duties, such as the duty of care and loyalty. The

---

<sup>41</sup>Ibid 5.

<sup>42</sup>Ibid 5.

<sup>43</sup>The Companies Act, No 71 of 2008, An Explanatory Guide (dti) 32.

<sup>44</sup>Davies and Others (n 15) 190-191.

<sup>45</sup>Deloitte (n 21) 29.

<sup>46</sup>Ibid

<sup>47</sup>Ibid

<sup>48</sup> German Stock Corporation Act

German Stock Corporation Act (AktG) contains specific provisions related to the governance and management of stock corporations, including rules on directors' duties, liability, and shareholder rights.

Generally, corporate governance on directors' duties and liabilities is a subject that **only little is** written about in Ethiopia. There is limited local research on corporate governance. To name some, Minga Negash has identified key areas that indicate the low standard of corporate governance in Ethiopia.<sup>49</sup> Among other things, he argues that:

- "The Commercial Code of 1960 does not provide an adequate legislative response to complex governance issues of the day, and the new draft corporate law has not yet been finalized.
- Fundamental international conventions, codes, and standards are not realized or adequately incorporated in the proclamations. The decrees and directives lack coherence and foresight and sometimes suffer from poor drafting. "

However, he left how these, and related matters should be addressed to future researchers.

Other researchers, like Kefene,<sup>50</sup> Mekonnen<sup>51</sup>, and Fikadu,<sup>52</sup> have attempted to cover some of the corporate governance issues in Ethiopian Share Companies. Kefene Gurum discussed the general powers, duties, and liability of directors. Mekonnen focused on the powers, duties, and responsibilities of the board of directors of financial institutions in Ethiopia. Fikadu dealt with protecting minority shareholders vis-a-vis corporate governance under the Ethiopian Commercial Code. All of them, however, did not appreciate problems surrounding core issues in corporate governance related to directors' duties and liabilities, such as responsibilities, the scope of application, composition, independence, and special board committees (including the audit committee, remuneration committee, and nomination committee) and their responsibilities, etc. of the board as well as transparency and disclosure in corporate governance. Mainly, they have not covered issues based on the newly reformed Commercial Code.

---

<sup>49</sup>Minga Negash, *Rethinking Corporate Governance in Ethiopia 2*.

<sup>50</sup>Kefene Gurmu, "Powers & Liabilities of Directors under the Commercial Code of Ethiopia"(2007) (unpublished Faculty of Law, AAU) 72.

<sup>51</sup>Mekonnen Shiferaw, "Rights, Duties and Responsibilities of Directors in Financial sector in Ethiopia: with special Emphasis on the Banking Sector" (2009) (unpublished, Addis Ababa university Law Library)10.

<sup>52</sup>Fekadu Petros, "Emerging Separation of ownership and control in Ethiopian Share Companies: Legal and Policy implications"(March 2010 Mizan Law Review, Vol 4. No 1)3.

Therefore, this research will be different from those previous related works. It will specifically focus on how the formulation of directors' duties and liabilities improves or impedes the governance of companies in Ethiopia by referring to some other selected countries' experience.

### **1.6 Methodology**

This study made use of a qualitative research methodology, which the researcher considered the most appropriate way to address the study's research questions due to its high level of flexibility. Additionally, the study included doctrinal research methods to examine the duties and liabilities of directors under the Ethiopian share company law. This involved analyzing relevant legal concepts and academic knowledge from literature in the area, as well as examining the experiences of selected countries' share company laws. Overall, this approach allowed for a thorough examination of the subject matter.

As this thesis involves a comparative analysis, it has consulted the company laws of the United Kingdom, Germany, and South Africa to gain relevant knowledge and insights from their better experiences. These particular countries were selected because they have developed a legal framework that covers Fiduciary Duties, Stakeholder Orientation, Corporate Governance Standards, Judicial Precedents for corporate governance, Shareholder Rights and Remedies, Disclosure and Reporting Requirements. These are considered to be a comprehensive and modern legal framework that governs companies and directors' duties.

### **1.7 Scope of the Research**

This study examines the law pertinent to the governance of companies in Ethiopia with specific reference to directors' duties and liabilities. The question of corporate governance about directors is a broad topic. Therefore, this study is intended to provide critical insight into the debate of directors' duties and liabilities only and does not purport to cover all possible issues relating to corporate governance.

### **1.8 Limitations of the Study**

In conducting this study, several limitations have been encountered, including factors that may have had a small impact on the study's results, limited time, and budget, as well as a shortage of internet access and relevant materials.

### **1.9 Significance of the study**

The main focus of the study is to analyze the Ethiopian share company laws in terms of the duties, responsibilities, liabilities, qualifications, and remunerations of the board of directors. Hence, the study aims to suggest solutions to improve the corporate governance of share companies. This research will provide valuable contributions to the legislative body, judges, lawyers, and investors interested in the area of corporate governance. Furthermore, it will serve as a reference material for those conducting further research in this field and will be a useful resource in the academic sphere.

### **1.10 Structure of the study**

The paper has four chapters. This first chapter provides a background of the study, and it addresses the problems of the study and questions it seeks to answer. The second chapter deals with the duties and liabilities of directors under Ethiopian law. The third chapter examines the duties and liabilities of directors of the selected countries' law. The last chapter discusses lessons learned from other countries' company law and practices to reform Ethiopian company law, particularly the duties and liabilities of company directors.

## Chapter Two

### Duties and Liabilities of Directors under Ethiopian Law

#### 2.1 Introductions

In this chapter, the duties, and liabilities of directors under Ethiopian law and the theoretical underpinning of the subject matter of the study will be addressed. The first section of this chapter will explore the nature and fundamental concept of corporate governance, including the meaning of the term and the role of the board of directors within the larger system. Additionally, the section will discuss the widely accepted theoretical stances on corporate governance to help readers better understand the topic. These concepts have been selected based on their effectiveness in addressing the core theoretical issues related to corporate governance. The next section of the chapter will focus on the board of directors' specific role in corporate governance. Finally, the chapter will conclude with an analysis and description of how Ethiopia's corporate governance laws, both past and present, impact directors' duties and liabilities.

#### 2.2 Corporate Governance in General

Before assessing the duties of directors objectively, it is important to have a solid understanding of corporate governance. The term "corporate governance" lacks a uniform definition due to its varied use by academics and professionals.<sup>53</sup> Though there is no uniform definition, several writers and legal documents provide various meanings of the concept.<sup>54</sup> The broad definition of corporate governance: "institutions that influence how business entities allocate resources and returns" and "the organizations and norms that shape expectations about the exercise of control of resources in firms" are frequently used by economists and social scientists.<sup>55</sup>

This idea emphasizes the significance of both formal corporate governance structures and informal practices that arise when regulatory limits are absent or ineffective.<sup>56</sup>

---

<sup>53</sup> Khan Humera, 'A literature review of corporate governance: In International Conference on E-business, management and Economics' (2011) vol. 25, no. 1, pp. 1-5 <<https://rb.gy/oytnnh>> accessed 4 February 2024

<sup>54</sup> Ibid

<sup>55</sup> Eswald W. SalaCluse 'Corporate Governance in the New Century' (2004) 25 No.3 The company Lawyer, p.69 (as cited Ahmed (n 18) 11)

<sup>56</sup> Ibid

However, the term used by corporate managers, investors, lawmakers, and lawyers is typically more restrictive than what one might think of when hearing the term "corporate governance." It refers to the system of rules and institutions that regulate a corporation's direction and management, as well as the interactions between its various stakeholders.<sup>57</sup> Based on the definitions mentioned above, it is possible to conclude that corporate governance indicates a set of institutions and structures aimed to effectively oversee and manage an organization's operations and strategies.

In addition, corporate governance ensures control and oversight over the company's management by focusing on investment policies, profit sharing, and decision-making procedures.<sup>58</sup> The way internal institutions like the board, which are constructed with experienced, impartial, knowledgeable directors, and external mechanisms like the stock and debt markets and the corporate control market function serve as evidence of the monitoring duty.<sup>59</sup>

Furthermore, when a principal delegates tasks to agents to safeguard his interests, governance issues can arise. This agency issue has been known for a while.<sup>60</sup> The shareholders elect a company's board of directors to represent their interests.<sup>61</sup> Members of professional bodies elect their council and select the committee of a club. As a result, a governing board needs to be elected following the constitution of each company. An organization's board of directors commonly establishes a governing body, such as a "council" or "committee," for oversight purposes.<sup>62</sup> The interactions between shareholders, directors, and particular management are emphasized when viewing corporate governance in a larger context via the perspective of the so-called corporate governance triangle.<sup>63</sup> This perspective heavily relies on the idea of separate ownership and control.

---

<sup>57</sup> Ibid

<sup>58</sup> Bob Tricker and Robert Ian Tricker, *Corporate governance: Principles, policies, and practices*, (Oxford University Press, 2015.)

<sup>59</sup> Tricker and Ian (n 83)

<sup>60</sup> Bob Tricker, *THE EVOLUTION OF CORPORATE GOVERNANCE* (Cambridge University Press, 2020)2

<sup>61</sup> Ibid

<sup>62</sup> Ibid

<sup>63</sup> Abigail Levrau, *Corporate governance and the board of directors: a qualitative-oriented inquiry into the determinants of board effectiveness*, (Diss. Ghent University, 2007.) 41 < <https://www.pdfdrive.com/corporate-governance-and-the-board-of-directors-e53316310.html> > accessed in 10 February 2024

## 2.3 The Nature of Corporate Governance

In the modern world, corporate governance is critical for the success of any business, irrespective of its size. It can determine whether a business will thrive or fail.<sup>64</sup> A company that capitalizes on good corporate governance will grow and survive. However, companies that lack a strong corporate governance framework run the risk of collapsing.<sup>65</sup> As a result, the current corporate scandals and crises involving large businesses have taught all nations a vital lesson.<sup>66</sup> Corporate governance has become one of the current challenges acknowledged in the literature. The frameworks used by different countries to regulate corporate governance differ. There is no common corporate governance model. Countries utilize different corporate governance principles and approaches. Apart from law, corporate governance is also studied in other academic disciplines.<sup>67</sup> Corporate governance is a topic that interests many other academic fields, including economics, management, business, and accounting.<sup>68</sup> The term "corporate governance" has been defined and explained by numerous academics in these fields. Consequently, the topic of corporation law is interdisciplinary. Altogether, corporate governance encompasses a broad range of theories and interpretations from multiple disciplines.<sup>69</sup>

## 2.4 Theories of Corporate Governance

There are many corporate governance concepts as there are academic disciplines that claim to be interested in them. The legal and economic perspectives on corporate governance, however, do not clash. Thus, the concepts that will be discussed in greater detail below have been selected according to how well they may address the fundamental issues associated with corporate governance. In reality, corporate governance theories play a major role in both legal and economic theories.<sup>70</sup> Theories are discussed in the subsequent sections.

---

<sup>64</sup> Alan Calder. *Corporate governance: A practical guide to the legal frameworks and international codes of practice*, (Kogan Page Publishers, 2008.)1< <https://rb.gy/s0uvsrl>> accessed in 10 February 2024

<sup>65</sup> Ibid

<sup>66</sup> BELAYNEW ASHAGRIE, 'CORPORATE GOVERNANCE IN BRANCHES OF FOREIGN COMPANIES IN ETHIOPIA: ANY DIFFERENT FROM LOCAL ETHIOPIAN COMPANIES?'(A Master's Thesis Submitted to School of Graduate Studies of Addis Ababa University in Partial Fulfillment of the Requirements of Masters of Law (LL.M),2014) 24

<sup>67</sup> Petri Mäntysaari, *Organising the firm: theories of commercial law, corporate governance and corporate law*, (Springer Science & Business Media, 2011.) 75< <https://rb.gy/omjqsq>> accessed in 6 march 2023

<sup>68</sup> Ibid

<sup>69</sup> Ibid

<sup>70</sup> Mäntysaari (n 92)

### 2.4.1 Agency Theory

The agency theory states that managers act as the company's "Agents." The company's primary objectives are determined by the directors or owners. The managers of the company are in charge of implementing these objectives into practice daily. Creating the structure and procedures for management is a necessary part of controlling it.<sup>71</sup> When one party, the principal, appoints or directs another, the agent, to carry out a duty that has been assigned to them, the Principal-Agent relationship comes into effect. The basic principle of the principal-agent relationship is that agents operate by extrinsic motivation and opportunism, and both sides maximize utility. Because there are uncertainties while observing the agent's action by the principal, the agent's assumption is important.<sup>72</sup> Under agency theory, owners are regarded as the principals. Principals, however, might not have the skills or knowledge necessary to achieve the objectives.<sup>73</sup> A formal agreement is formed between the principal and the agent once the principal gives the managers authorization to work as "Agents." As per the provisions of the agency agreement, the agent must act honestly. He has to defend the objectives and protect the principal's interests.<sup>74</sup> Thus, the primary argument of the agency theory is that management behaves differently from what shareholders expect to maximize profit. Without sufficient mechanisms for timely disclosures, oversight, and monitoring, the dispersed principals might not be able to fight this.

The agency theory is not without critics. To begin with, the aim of this theory cannot be accomplished on its whole since shareholders are less likely to be successful in identifying agents who abuse trade-offs.<sup>75</sup> Furthermore, even if shareholders have a right to sufficient information for efficient control (of the corporation), equity investors hardly ever receive the information.<sup>76</sup> They also have fewer options for acting against director boards.<sup>77</sup>

---

<sup>71</sup> Glinkowska, Beata, and Boguslaw Kaczmarek. 'Classical and modern concepts of corporate governance (Stewardship Theory and Agency Theory)' (2015): Management 84.

<sup>72</sup> Hong Bo, and Ciaran Driver 'Agency Theory, Corporate Governance and Finance' University of London School of Oriental and African Studies

<[https://www.researchgate.net/publication/273979161\\_Agency\\_Theory\\_Corporate\\_Governance\\_and\\_Finance](https://www.researchgate.net/publication/273979161_Agency_Theory_Corporate_Governance_and_Finance)> accessed in 6 march 2024

<sup>73</sup> Ibid

<sup>74</sup> John Roberts, *Agency theory, ethics and corporate governance. Corporate Governance: Does Any Size Fit?*. (Emerald Group Publishing Limited, 2005) 2. <<https://rb.gy/3tzvbr>> accessed in 8 march 2024

<sup>75</sup> Ibid

<sup>76</sup> Thomas Clarke, 'Theories of corporate governance: The Philosophical Foundations of Corporate Governance' (2004) Oxon 12.4 244-266.

To add more, since this theory's foundation is the idea that directors will maximize value, evaluating utility might be challenging.<sup>78</sup> The self-interest assumption is also criticized for failing to consider the reality that conflicting market assumptions frequently impose restrictions on actors' behavior. Perhaps the most well-known criticism of this theory is its restricted focus on shareholders as the primary stakeholder group deserving of attention from corporate managers in information delivery and transparent, accountable governance.<sup>79</sup>

#### 2.4.2 Stockholder/shareholder Theory

According to this theory, which is stockholders and shareholders are regarded as the corporation's owners.<sup>80</sup> They are free to dispose of this asset however they like. They want to extract the most profit possible out of this property.<sup>81</sup> Corporate owners act in this way because they want to get a return on their investment. The board ensures that the company complies with the ethical and legal requirements set out by the government.<sup>82</sup> This restricted duty has been expanded to include keeping an eye on the corporation's activities and management. Consequently, the directors are responsible for any harm that is caused to their company. Increasing shareholder wealth is a manager's main duty.<sup>83</sup>

The primary criticisms of this theory are that, in its "extreme" version, the shareholder model rejects the idea that businesspeople have any societal duties in addition to their fiduciary duty to maximize shareholder value while following the law and fundamental ethical principles.<sup>84</sup> As a result, any business initiatives addressing social or environmental issues are seen as instances of

---

<<https://www.academia.edu/download/6742768/theoriesofcorporategovernancepreface.pdf>> accessed in 8 march 2024

<sup>77</sup> Ibid

<sup>78</sup> Lex Donaldson and Davis H. James, 'Stewardship theory or agency theory: CEO governance and shareholder returns' (1991) Australian Journal of management 16.1 49-64.

<<https://www.academia.edu/download/33569543/rprnts.stewardshiporagency.pdf>> accessed in 10 march 2024

<sup>79</sup> Ibid

<sup>80</sup> Joseph Heath and Wayne Norman, 'Stakeholder Theory, Corporate Governance and Public Management: What can the History of State-Run Enterprises Teach us in the Post-Enron era?', (2004) 53(3), 247–265 <<https://rb.gy/dkiunm>> accessed in 6 march 2023

<sup>81</sup> Ibid

<sup>82</sup> Ibid

<sup>83</sup> Ibid

<sup>84</sup> Michel Aglietta and Reberieux Antoine. *Corporate governance adrift: a critique of shareholder value*. (Edward Elgar Publishing, 2005). <<https://rb.gy/gp4hvf>> accessed in 15 march 2023

agency issues where managers abuse the resources of the principals and act in their interests rather than the interests of shareholders.<sup>85</sup>

### **2.4.3 Theories of Convergence**

Proponents of this theory argued that as markets become more globalized, corporate governance is likely to converge.<sup>86</sup> On the other hand, opponents of convergence have a wealth of facts to back up their arguments. They provide the factor of cultural differentiation, contending that it is difficult to unify two distinct cultures under a single corporate governance model, and as a result, convergence theory is impossible.<sup>87</sup> The legal argument against corporate governance convergence points out that corporate law is closely linked to other legal domains, including banking, labor, tax, and competition law, in addition to social custom. These legal domains would be very difficult to change all at once due to the multiple interests that have been built up around them.<sup>88</sup> Convergence theories are challenging. The differences between the country's political, legal, cultural, and economic systems are the cause. Thus, unless countries address all of the obstacles to convergence, convergence will still be unattainable. Unfortunately, this appears to be exceedingly challenging. As a result, every country will keep appropriating its style following its requirements.<sup>89</sup>

### **2.4.4 Stakeholder Theory**

The idea argues that the business should be considered as an input-output model considering all interested parties involved, including creditors, employees, consumers, suppliers, the local community, and the government.<sup>90</sup> They believe that a company works for them as well as its stockholders.<sup>91</sup> Everybody involved has their own set of interests. It is the manager's and the company's responsibility to mediate conflicts between the interests of these numerous stakeholders because these parties' interests occasionally conflict. The concerned parties are

---

<sup>85</sup> Ibid

<sup>86</sup> Hassan Ahmed SHIRWA and Assist. Prof. Dr. Murat ONUK 'Convergence of Corporate Governance Models: The Arguments in Favor and Against its Possibility'(2020) Yeditepe University, MBA Student Review 250-255 <<https://rb.gy/5kjfsz> > accessed in 15 march 2023

<sup>87</sup> Ibid

<sup>88</sup> Ibid

<sup>89</sup> Ibid

<sup>90</sup> Thomas Donaldson, and Lee E. Preston,'The stakeholder theory of the corporation: Concepts, evidence, and implications'(1995) Academy of management Review 65-91. <<https://sci-hub.hkvisa.net/10.5465/AMR.1995.9503271992>> accessed in 20 march 2023

<sup>91</sup> Ibid

united with one another.<sup>92</sup> Thus, companies need to make an effort to match their interests with those of other stakeholders. Therefore, managers must act with integrity and be trusted representatives of all parties concerned, not just stockholders. They have a crucial role to play in this. First of all, corporations cannot implement this principle in their daily operations.<sup>93</sup> The second criticism is that there is less likelihood of a connection between the concept of a stakeholder and corporate governance, and it is more challenging to identify. The assertion that stockholders have no particular status under corporate law is likewise false.<sup>94</sup>

Although creditors may also use their contracts to exercise control, only shareholders have the right to bring legal action on behalf of a solvent corporation.<sup>95</sup> The board's fiduciary duties extend "to the corporation and its shareholders," and shareholders are the only group with the right to vote for the board and approve significant corporate transactions. These legal rights are significant and should not be disregarded.<sup>96</sup>

#### **2.4.5 Stewardship Theory**

This value-based theory uses the term to refer to a corporation acting as a guardian; in the absence of the owner, managers, and employees are in charge of protecting its assets, interests, and property.<sup>97</sup> They must take the best possible care of the company and refrain from using the property for personal gain. The company should be run by the managers as if it were their own business.<sup>98</sup> They act as stewards rather than agents in the classic sense. The principal's goal drives the managers, and their behavior is cooperative, dependable, and pro-organizational. According to this approach, standards are formed initially by defining and formulating values.<sup>99</sup> The next stage is to create training programs that aid in excellence. Finally, moral reinforcement is necessary to close any gaps in morality.<sup>100</sup> There are similarities and distinctions between the

---

<sup>92</sup> Ibid

<sup>93</sup> Stephen Letza, 'Corporate governance theorising: limits, critics and alternatives'(2008) International Journal of law and management<<https://www.emerald.com/insight/content/doi/10.1108/03090550810852086/full/html>> accessed in 26 march 2023

<sup>94</sup> Ibid

<sup>95</sup> Ibid

<sup>96</sup> Heath and Norman (n 104)

<sup>97</sup> Lex Donaldson, and Davis H James, 'Stewardship theory or agency theory: CEO governance and shareholder returns' (1991) Australian Journal of management 49-64<<https://journals.sagepub.com/doi/abs/10.1177/031289629101600103>> accessed in 29 march 2023

<sup>98</sup> Ibid

<sup>99</sup> Ibid

<sup>100</sup> Ibid

agency theory and the stewardship theory. While managers act as stewards under the stewardship concept, the agency theory implies that they represent the owners of the organization as their agents.<sup>101</sup> Under the agency theory, the approach to governance is sociological and psychological, while under the other, it is materialistic; the behavioral pattern under the agency theory is individualistic, opportunistic, and self-serving, while under the other, it is collectivist, pro-organizational, and dependable.<sup>102</sup> Regarding their organizational interests, managers and principals vary significantly from one another; whereas they converge under the second theory, they diverge under the former.<sup>103</sup> In the first scenario, managers are only driven by their own goals, whereas in the second scenario, they are directed by the principal's goals. In addition, managers' organizational responsibilities are to monitor and regulate them, in contrast to the agency theory, which emphasizes empowerment and facilitation.<sup>104</sup> Owners in agencies have a risk-averse mindset, as opposed to accepting and managing risk as it does in the second organization. The principal-manager relationship is relationship-based in the latter company, but control is the only factor in these organizations.<sup>105</sup>

In summary, the basis of all five of the aforementioned ideas is the idea that the firm's founders get a return on their investment. The various types of corporate governance that are currently in use have been influenced by corporate structures and global economies. These models have evolved as a result of convention or in response to external elements such as politics, law, and society as well as philosophy. Because of the quick changes occurring in the internal and external business environments, corporate governance is always evolving. External environmental elements include financial backing, new ventures, business collaborations, technical advancements, mergers, and acquisitions. The company's aim to increase revenues, shareholders, and stakeholders are examples of internal environmental elements. All of these environmental problems have a direct or indirect impact on changes in corporate governance. The corporate governance frameworks of different countries might differ due to factors such as political, cultural, and economic environments.

---

<sup>101</sup> Alan Calder, *Corporate governance: A practical guide to the legal frameworks and international codes of practice*. (Kogan Page Publishers, 2008) <<https://rb.gy/u4pjrb>> accessed in 29 march 2023

<sup>102</sup> Ibid

<sup>103</sup> Ibid

<sup>104</sup> Ibid

<sup>105</sup> Ibid

## 2.5 Corporate Governance and the Board of Directors

The corporation is the hub for agreements between parties with conflicting interests and opportunistic tendencies.<sup>106</sup> Most discussions of corporate governance situate on agreements between company management and residual risk bearers.<sup>107</sup> Corporate governance structures help reduce the transaction costs associated with the specialization of organizational functions by serving as a collection of institutional arrangements that tend to align the interests of management and shareholders who bear risk.<sup>108</sup>

The corporate governance structure is composed of several components, one of which is the board of directors. The market for corporate control, the labour market for managers, the easy alienability of shares, competition in the capital and product markets, and corporation law are further factors to consider.<sup>109</sup> Another important governance structure that is said to reduce agency costs is the corporate organization's division of decision control, which is the duty of the board, from decision management, which is carried out by managers.<sup>110</sup> Shareholders will be ready to put their money at risk under the guidance of self-interested managers as long as directors (whether corporate insiders or independent outsiders) are concerned with the market's assessment of their capacity to deliver the services of decision control.<sup>111</sup> The board of directors is a specialized governance structure that reduces transaction costs for this specific set of manager-shareholder contracts since it can hire, fire, and compensate management at regular or irregular intervals.<sup>112</sup>

---

<sup>106</sup> Barry D Baysinger, and Butler N Henry, 'Corporate governance and the board of directors: Performance effects of changes in board composition' (2019) *Corporate Governance*. Gower, 215-238 <<http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.962.1155&rep=rep1&type=pdf>> accessed in 2 April 2024

<sup>107</sup> Ibid

<sup>108</sup> Ibid

<sup>109</sup> Ibid

<sup>110</sup> Naciti Valeria, 'Corporate governance and board of directors: The effect of a board composition on firm sustainability performance' (2019)" *Journal of Cleaner Production* 237 <<https://www.sciencedirect.com/science/article/pii/S0959652619325879>> accessed in 2 April 2024

<sup>111</sup> Ibid

<sup>112</sup> Baysinger and Henry (n 127)

## 2.6 Duties and Liabilities of Directors under the Ethiopian Corporate Governance Code

Having oversight of the direction, conduct, management, or supervision of the company's affairs is what is meant by the definition of a director.<sup>113</sup> Article 296 of the new Commercial Code provides a brief description of the members of the board of directors however does not define a director.<sup>114</sup> Unlike the repealed Commercial Code that did not. One of the new commercial law's concerns is that it doesn't define what a director is. Several countries have laws that define what a director is and who qualifies for that category. Nevertheless, a director is "any member of a bank's board of directors, regardless of his title," as stated in Banking Business Proclamation No. 592/2008.<sup>115</sup> Therefore, it is essential to take into consideration the duties and nature of the role when determining whether a person meets the requirements to be a director. A person is considered a director in the eyes of the law if they serve on a board and carries out the duties of a director.

Articles 347 through 367 of the commercial codes, which were repealed, cover the twenty-one requirements that govern the board of directors. These regulations address a wide range of topics, such as minority shareholder protection and the appointment, compensation, termination, duties, and liabilities of the board of directors. However, as experts and businesses discovered over time, the Ethiopian company law lacked adequate legislative provisions on governance concerns of the division of supervisory and management duties, as well as on the makeup, independence, and compensation of the board of directors.<sup>116</sup> This, along with other challenges associated with modernity, forced the Ethiopian parliament to revise the commercial code that had been in place for six decades.<sup>117</sup> As a result, in 2021, the Federal Democratic Republic of Ethiopia (FDRE) Commercial Code (Proclamation No. 1243/2021) came into effect, bringing with it many advantageous modifications, such as the creation of a two-tier board of directors structure for share companies.<sup>118</sup> According to the new business law, directors have the right to make business

---

<sup>113</sup> Rita D. Kosnik, 'Greenmail: A study of board performance in corporate governance.' (1987) *Administrative science quarterly* 163-185. < <https://www.jstor.org/stable/pdf/2393124.pdf> > accessed in 5 April 2024

<sup>114</sup> Misganaw Belete, THE NEW ETHIOPIAN COMMERCIAL CODE: UNCOVERING THE MAJOR CHANGES IN COMPOSITION, ROLE, AND ACCOUNTABILITY OF THE BOARD OF DIRECTORS( 2022) *Commercial Law Blog* < <https://www.abyssinialaw.com/blog-posts/itemlist/user/9359-misganawbelete> > accessed in 5 April 2024

<sup>115</sup> Banking Business Proclamation, 2008, Proclamation No. 592, Federal Neg. Gaz. Year 14, No 57

<sup>116</sup> Belete (n 135)

<sup>117</sup> Ibid

<sup>118</sup> Ibid

decisions in good faith (Business judgment rule), which helps directors do their work without embarrassment. Accordingly, the duties and liabilities of the board of directors under Ethiopia's present corporate governance rules will be covered in the following section.

### **2.6.1 Duties of Directors under the Ethiopian Corporate Governance Code**

Directors' duties are the acts that they are required by law and morals to carry out. A director's obligations usually relate to their authorities and liabilities. The obligations of directors under Ethiopia's commercial code will be discussed in this section. It is stated that directors have three different responsibilities: obedience, diligence, and loyalty.<sup>119</sup> Regarding diligence, directors must remain due to a duty to exert reasonable care, prudence, and loyalty to behave honestly and honourably.<sup>120</sup> As for obedience, directors must have a duty to keep within the authority of the firm and board of directors.<sup>121</sup> The board of directors is required by law to carry out decisions made by the general assembly or by the association's articles of incorporation, as well as to appropriately manage the association's financial matters, establish appropriate procedures to keep the association from being exposed to risk, appropriately manage the association's significant accounting and other documents, and establish appropriate procedures to avoid the association from having to pay off its debts. This is stated in Article 315 of the Commercial Law. They have to file for bankruptcy when their capacity is diminished. Thus, the primary duty of the board is to provide the association with the strategic leadership it needs to run a capable and effective business. The board of directors works together under the association's rules and regulations and has the authority to manage the activities of the organization.

In addition, Articles 316 through 318 of the new commercial code explain the fundamental duty of the board of directors. They fall under three categories: the duty of care and diligence, the duty of loyalty, and the duty to apply independent judgment. Additional director duties are also provided under Articles 318 through 322 of the new business laws.

---

<sup>119</sup> Harry C. Henn, *Laws of Corporation* (New York, West Group 1983) 3rd ed 612

<sup>120</sup> Ibid

<sup>121</sup> Ibid

### ***2.6.1.1 Duty of loyalty***

The fundamental principle of duty of loyalty is that directors should act in the organization's best interests, not their own.<sup>122</sup> Avoiding transactions that create a conflict of interest is the simplest way to keep this commitment. These types of transactions can be referred to as "self-dealing" transactions.<sup>123</sup> It is said that because the directors are negotiating among themselves, the decision that is beneficial to the company may not be achieved. Because complete prohibition of self-dealing transactions might not be possible, especially for smaller businesses, most countries provide the alternative of having them verified by an impartial decision-maker.<sup>124</sup> These decision-makers may be disinterested shareholders, disinterested directors, or occasionally both.

Article 316 (1) of the new Commercial Code provides that Directors must behave in a way that they believe, in good faith, will most likely contribute to the company's success, and they must act in the best interests of all of the company's shareholders.<sup>125</sup> Sub-article two of the same article also requires boards to consider the long-term interests of the company, as well as the interests of its financiers, employees, and the community and environment.<sup>126</sup> Therefore, when the association achieves greater achievement, the Board of Directors for the Association's Duty of Loyalty and Trust will be more effective in acting on their convictions. Moreover, every shareholder's usability increases. Article 316 seems to be promulgated to enhance the business. Among the obligations mentioned in this section is the board of directors' duty.

### ***2.6.1.2. Duty to Exercise Independent Judgment***

The new Commercial Code's Article 317 clause outlines many responsibilities and demonstrates the gravity of the board of directors' duties.<sup>127</sup> Unless there are specific restrictions specified in the memorandum of association or by agreement with the corporation, members of the board of directors shall exercise independent and unbiased judgment in carrying out their duties.<sup>128</sup> However, a director's independence does not shield them from legal consequences for any

---

<sup>122</sup> Rashid Zaman, 'Fiduciary duty or loyalty? Evidence from co-opted boards and corporate misconduct.' (2021) *Journal of Corporate Finance* 70 <<https://rb.gy/lrtwov>> accessed in 6 April 2024

<sup>123</sup> *Ibid*

<sup>124</sup> *Ibid*

<sup>125</sup> Article 316 of The FDRE Commercial Code

<sup>126</sup> *Ibid*

<sup>127</sup> Article 317 (1 and 2) of The FDRE Commercial Code

<sup>128</sup> *Ibid*

activities they do that infringe the law, the decisions of the General Assembly, or the association's memorandums.<sup>129</sup>

It should be noted that the director freely and consciously refers to the association's articles of incorporation; this in no way implies that the General Assembly acted unlawfully in its decision. When it exercises its discretion, it does so freely and in compliance with the law or the association's rules and regulations.

### ***2.6.1.3 Duty of Care and Diligence***

According to Article 318 of the new Commercial Code, Board members must perform responsibly and diligently. Members of the board of directors are obligated to carry out their responsibilities diligently.<sup>130</sup> The director's duty is measured by the care and expertise that a company director must show, as well as the diligence that may be anticipated of a person performing the duties of a company director.<sup>131</sup> It states that the benchmark is based on the whole amount of knowledge, ability, and prudence that a responsible board member should possess. This criterion or measurement is relative and subjective.<sup>132</sup>

Therefore, directors must show care and skill in carrying out their duties. The term "care" refers to the responsibility to pay attention.<sup>133</sup> Directors must therefore inform them of all relevant information before acting.<sup>134</sup> After receiving this information, employees must exercise caution when carrying out their duties. If they act carelessly, they will be liable for breaching the duty of care; however, simple mistakes in judgment or imprudent actions may not always constitute a duty violation.<sup>135</sup> To fulfil his duty of care, a director must keep a close eye on the activities of the company where he serves. If a director's failure to fulfil a duty could result in a violation of his duty of care, then the director is accountable for his actions.<sup>136</sup>

---

<sup>129</sup> Belete (n 135)

<sup>130</sup> Article 318 (1 and 2) of The FDRE Commercial Code

<sup>131</sup> Ibid

<sup>132</sup> Belete (n 135)

<sup>133</sup> Stephen Griffin, *Company Law: Fundamental Principles* 3rd ed (London, Pearson Education Limited, 1991) 260

<sup>134</sup> Ibid

<sup>135</sup> Ibid

<sup>136</sup> Ibid

#### ***2.6.1.4 Duty to avoid conflict of interest***

Another commitment that prevents directors from using the company's resources, information, or commercial opportunities for their own or others' profit is the duty to avoid conflicts of interest. The new Commercial Code comprises two categories of provisions that prohibit and regulate transactions, which aim to prevent conflicts of interest between a company and directors. Directors are prohibited from entering into loan agreements with enterprises and from participating as partners in competing companies with joint and several liabilities.<sup>137</sup> or engage in competition with the company directly or indirectly; nevertheless, a director may enter a transaction with a company only after receiving prior consent from the General Assembly.<sup>138</sup>

#### ***2.6.1.5 Duty to Disclose Conflict of Interest***

According to article 321 of the new commercial code, every condition that may result in a conflict between his and the company's interests must be declared to the board of directors by each director.<sup>139</sup> A corporation director must disclose to the other directors the nature and scope of any direct or indirect interest he may have in a proposed transaction, a signed contract, or any other relationship with the company.<sup>140</sup> Once a situation that potentially results in a conflict of interest is recognized, it must be declared based on this provision Article.<sup>141</sup> The prohibition can be lifted and permission granted by the board of directors or the association's general meeting. If the issue is likely to result in a conflict of interest between the board member and the association, or if the anticipated contract is related to the board member's interests, the other directors should be provided with a thorough explanation. The board should ratify the arrangement between the association and those connected to it. He/she mentioned that Article 306 prevents a board member with a conflict of interest from casting a vote.

#### ***2.6.1.6 Benefits from Third Parties***

According to Article 322 of the new commercial code, a director of a corporation is not allowed to accept a gift or another sort of benefit from a third party as a result of his or her position as a director without the permission of the non-beneficiary director or the shareholders.<sup>142</sup> This article

---

<sup>137</sup> Article 319-320 of The FDRE Commercial Code

<sup>138</sup> Ibid

<sup>139</sup> Article 321 of The FDRE Commercial Code

<sup>140</sup> Ibid

<sup>141</sup> Ibid

<sup>142</sup> Ibid Article 322

does not apply if receiving the gift or benefit cannot reasonably be expected to result in a conflict of interest. A person who stops serving as a corporate director continues to have to obey Sub-Article (1) of this Article.<sup>143</sup>

As a result, the duties mentioned above constitute the board of directors' primary functions. These board members' obligations and responsibilities are generally recognized by the common law and civil law legal systems, which include the company statutes that are in use in the UK, South Africa, and Germany. Ethiopia has not tested them out. Therefore, it might be difficult to apply them in the future.

## **2.6.2. Liabilities of Directors under the Ethiopian Corporate Governance Code**

Board members might face legal consequences in both civil and criminal courts for engaging in inappropriate activity while carrying out their official duties, regardless of whether they are corporate members or not.<sup>144</sup> Regarding the board's civil liabilities, directors act as the company's trustees and agents, and they have a duty to the company under the terms of the meeting decisions and regulations as well as by the law.<sup>145</sup> For the breach or non-performance of these duties, directors are equally and severally liable to the company, its shareholders, and any third-party creditors.<sup>146</sup>

### ***2.6.2.1 Liability towards the Company***

Article 325 of the new commercial law explicitly defines directors' duties to the company. In light of this, directors are jointly and severally liable to the company for losses caused by their negligence.<sup>147</sup> As a result, the company may assert any or all of them and seek full compensation for damages. The law does not provide an objective standard of culpability in this regard.<sup>148</sup> However, according to sub-article 2 of Article 325, directors must carry the burden of proof to prove that they have acted with due care and diligence.<sup>149</sup> As a result, they would only be able to avoid liability if they could demonstrate that their actions were carried out with due care and effort. Article 327 of the same Code expands on this possible reason for directors. A director

---

<sup>143</sup> Ibid

<sup>144</sup> Belete (n 135)

<sup>145</sup> Ibid

<sup>146</sup> Ibid

<sup>147</sup> Article 325 of The FDRE Commercial Code

<sup>148</sup> Belete (n 135)

<sup>149</sup> Article 325(2) of The FDRE Commercial Code

who raised dissatisfaction with a business decision in good faith and immediately informed the external auditor may not be held liable.<sup>150</sup>

#### ***2.6.2.2 Liability to Shareholders***

The company's shareholders may hold board members liable for losses made to one or more shareholders. The Ethiopian Commercial Code allows shareholders the authority to bring a lawsuit against board members in Article 333.<sup>151</sup> In this case, the law does not state whether shareholders can sue the directors for joint and several liability. However, since Article 325(1)'s phrase implies that directors are jointly and severally liable to the corporation, it is reasonable to assume that the objective of the legislature was the same for directors' duties to shareholders.<sup>152</sup>

#### ***2.6.2.3 Liability to Creditors***

Those who are entitled to payments from the company are known as creditors. Directors are responsible to the company's creditors for any loss in assets they create in situations when the company's assets are insufficient to pay creditors because one of their duties is to protect the company's assets.<sup>153</sup> Other parties have the right to use the company's assets to settle their claims. If the company's assets aren't enough to satisfy its debts and the directors are at fault, the claimant can sue them in private court.<sup>154</sup> In this particular instance, the company's decision to drop its litigation against the directors does not waive the creditors' right to sue them.

#### ***2.6.2.4 Criminal Liability of the Board of Directors***

Company directors who break their fiduciary duties or act in a way that harms the corporation's interests are also liable to criminal penalties in addition to civil liability.<sup>155</sup> Article 702(1) of the Ethiopian Criminal Code states that anyone who is obligated by law or contract to monitor or manage another person's property rights and intentionally harms those property interests by misusing their authority or neglecting to carry out their duties faces a fine or simple imprisonment.<sup>156</sup> If the crime were committed negligently, the offender would be fined or placed in simple jail for six months.<sup>157</sup> If the criminal committed the violation with the intent to benefit

---

<sup>150</sup> Ibid Article 327

<sup>151</sup> Ibid Article 333

<sup>152</sup> Belete (n 135)

<sup>153</sup> Article 329 of The FDRE Commercial Code

<sup>154</sup> Ibid

<sup>155</sup> Belete (n 135)

<sup>156</sup> Article 702 of The Criminal Code of the Federal Democratic Republic of Ethiopia 2004

<sup>157</sup> Ibid

themselves or another party financially, they are facing a minimum one-year sentence in ordinary jail and a maximum fine of 30,000 Birr.<sup>158</sup> Thus, Depending on the situation, the punishment could be more severe.

## **2.7 Conclusion**

Therefore, Ethiopia's existing corporate governance law clearly defined the board of directors' role and responsibility to resolve governance issues in the new code, among other principles. Except for the duties and authority delegated to directors by the shareholders' general meeting and the memorandum of association, the new code includes a list of instances of various powers. The new Commercial Code establishes stringent requirements to protect companies, shareholders, and creditors from errors of directors, while also broadening the scope of board members' liability by including their personal property. Unless it can be proven differently, the directors will be held liable for any harm they cause to the company, both criminal and civil liabilities. In this sense, even if the company tolerates or is hesitant to take action against the board members, shareholders have the power to demand an audit and file individual lawsuits against them.

---

<sup>158</sup> Ibid

## Chapter Three

### Duties and Liabilities of Directors under the Foreign Jurisdictions

#### 3.1. Introduction

The first section of this chapter will provide a general overview of the company laws in Germany, the UK, and South Africa. It aims to equip the reader with an understanding of the current company laws in these countries and will conclude by providing details regarding the development of corporate laws in these nations. The chapter will also examine the existing company laws in different countries, offering the reader a comprehensive knowledge of the legal framework. Additionally, it will explain how previous and current corporate governance laws in the selected countries affect the duties and liabilities of directors. Subsequent sections will cover relevant cases and statutes that are significant for understanding the duties and liabilities of the board of directors in these countries. Finally, the chapter will review the duties and liabilities of directors under company laws and provide examples of situations that can be used to improve the legal framework governing the responsibilities and liabilities of the board of directors under corporate governance.

#### 3.2 The South African Company Law: An Overview

The initial pieces of legislation establishing company law in South Africa were the Joint Stock Companies Limited Liabilities Act No. 23 of 1861 of the Cape Colony, which was a perfect copy of similar English legislation.<sup>159</sup> The first national company law, the Union Companies Act, was created in 1926 and is amended periodically to reflect the most recent English legislation.<sup>160</sup> The 1926 Act has been replaced by the Companies Act No. 61 of 1973, which mainly follows English law despite attempts to modernize and drive in a more South African direction.<sup>161</sup> The Companies Act of 1973 in South Africa was in force for over thirty years before the 2008

---

<sup>159</sup> GENERAL NOTICE, 'South African Company Law for the 21st Century Guidelines for Corporate Law Reform' (2004) STAATSKOERANT, NOTICE 11 83 OF 2004 <[https://www.gov.za/sites/default/files/gcis\\_document/201409/26493gen1183a.pdf](https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf)> accessed in 15 April 2024

<sup>160</sup> Michele Havenga, 'Directors' fiduciary duties under our future company-law regime.', (1997) S. Afr. Mercantile LJ 9 310. <[https://heinonline.org/hol-cgi-bin/get\\_pdf.cgi?handle=hein.journals/safrmerlj9&section=36](https://heinonline.org/hol-cgi-bin/get_pdf.cgi?handle=hein.journals/safrmerlj9&section=36)> accessed in 15 April 2024

<sup>161</sup> General Note (n 180)

Company Act's thorough review to reflect significant changes in South Africa and abroad.<sup>162</sup> Thus, South Africa has had three different Companies act as a single nation.<sup>163</sup> The Companies Act 71 of 2008, the most recent Act, came into force on May 1, 2011, following the enactment of the first Companies Act in 1926 and the second in 1973. The Company's Act was changed almost every year following 1973, some of the modifications being more substantial than others.<sup>164</sup> These changes made sure that South African company law kept up with changing business practices and developments.

Notably, the duties and liabilities of a company's directors have periodically been a source of contention in company law, since, until recently, this field of law was incorporated into South African common law and, for the most part, was not codified in any statute.<sup>165</sup> The previous Companies Act, No. 61 of 1973 (the "1973 Act"), followed English law and did not attempt to codify the law governing directors' duties and liabilities. Instead, it left this to be decided by the courts.<sup>166</sup> In this regard, the cases established over the years have not always been consistent. Currently, the principal legislation governing corporate governance is the Companies Act, No. 71 of 2008, and the Companies Regulations 2011.

### **3.2.1 The South African Companies Act 71 of 2008**

Since the new Companies Act No. 71 of 2008 (the "2008 Act") entered into force, several directors have questioned whether they recognize and appreciate what is expected of them in managing their companies.<sup>167</sup> Some have even questioned whether it is still advisable to serve as a director given perceived increases in the responsibility falling on them in their function as directors, as well as potential personal liabilities.<sup>168</sup> Company directors' responsibilities have historically been ambiguous in company law, as this area was previously based on South African common law and not formalized in any statute until recently.<sup>169</sup> To closely follow English law,

---

<sup>162</sup> General Note (n 180)

<sup>163</sup> Dennis Davis and Walter Geach, *Companies and Other Business Structures in South Africa*, (3<sup>rd</sup> ed, Oxford University Press Southern Africa (Pty) Ltd 2013 ) 26

<sup>164</sup> Ibid

<sup>165</sup> Cliffe Dekker Hofmeyr, 'Corporate Governance: A Guide for Directors'(2021)CDH <<https://www.cliffedekkerhofmeyr.com/export/sites/cdh/en/sectors/downloads/Corporate-Governance-A-Directors-Guide.pdf>> accessed in 15 April 2024

<sup>166</sup> Ibid

<sup>167</sup> Ibid

<sup>168</sup> Ibid

<sup>169</sup> Ibid

the prior Companies Act, No. 61 of 1973 (the "1973 Act") did not attempt to codify the law relating to directors' duty, instead leaving this to the courts.<sup>170</sup> In this regard, the established cases have not always been consistently aligned.

The responsibilities are important because they significantly contribute to protecting and advancing corporate governance ethics and values.<sup>171</sup> A significant percentage of corporate law eventually deals with corporate governance.<sup>172</sup> While the 2008 Act as it exists now has provisions that are more focused on directors' general duties and are comparable to the Common Law duties of directors, some of the early drafts of the 2008 Act attempted to codify the majority of directors' duties.<sup>173</sup> The provisions related to directors under the 2008 Act must be fully understood by taking into consideration the Companies Regulations, 2011 (referred to as the "Regulations") promulgated under the 2008 Act, as well as the applicable common law rules.<sup>174</sup> Recent case law developed under the 2008 Act revealed that the Act only gives a partial codification of all directors' authority and obligations.<sup>175</sup>

Prescribed officers and members of board committees or audit committees of corporations have the same duties and liabilities.<sup>176</sup> This includes (non-director) officials co-opted to such committees, regardless of whether they are members of the company's board of directors.<sup>177</sup> The 2008 Act is stronger than common law in some circumstances when it comes to directors' duties, and because statutory law takes precedence over common law in cases of inconsistency, it is vital to understand how the 2008 Act has made some duties more rigorous or onerous than before; Remarkably, these obligations have been a part of South African law for many years (both before

---

<sup>170</sup> CDH (n 187)

<sup>171</sup> Johan J Henning, 'The South African close corporation under the Companies Act of 2008.' (2009) *Amicus Curiae* <[https://sas-space.sas.ac.uk/2911/1/Amicus80\\_Henning.pdf](https://sas-space.sas.ac.uk/2911/1/Amicus80_Henning.pdf)> accessed in 20 April 2024

<sup>172</sup> CDH (n 187)

<sup>173</sup> Linda Muswaka, 'Corporate governance under the South African Companies Act: a critique' (2012) *Proceedings of World Business and Economics Research Conference*. <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2184678](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2184678)> accessed in 20 April 2024

<sup>174</sup> CDH (n 187)

<sup>175</sup> *Ibid*

<sup>176</sup> Jacqueline Yeats, 'The effective and proper exercise of appraisal rights under the South African Companies Act, 2008: developing a strategic approach through a study of comparable foreign law' (Thesis presented for the degree of DOCTOR OF PHILOSOPHY, Commercial Law Department at UNIVERSITY OF CAPE Town, 2016) <[https://open.uct.ac.za/bitstream/handle/11427/20301/thesis\\_law\\_2016\\_years\\_jacqueline.pdf?sequence=1](https://open.uct.ac.za/bitstream/handle/11427/20301/thesis_law_2016_years_jacqueline.pdf?sequence=1)> accessed in 25 July 2022

<sup>177</sup> *Ibid*

and during the development of case law under the 1973 Act).<sup>178</sup> After specifying the duties, there is a perception that they may be more accessible and easily enforceable. Shareholders and other stakeholders of a company may be able to rely on the statutory causes of action provided for by the 2008 Act, rather than having to base their causes of action on compliance.<sup>179</sup> This idea has been confirmed in practice by the cases that have been decided since the beginning of the Act in 2008.

The 2008 Act now includes numerous and broad personal liability provisions in sections 77 (liability to the company), 218(2) (liability to any third parties for any violations of the 2008 Act), and other places.<sup>180</sup> This is critical since breaches of duties are now associated with these rules. Personal liability existed under both the 1973 Act and common law, but the 2008 Act included legislative remedies that made it easier to file claims against directors who breached their duties.<sup>181</sup> Furthermore, according to a recent decision, a third party (such as a creditor) should be able to directly sue a director under section 218(2) for losses and damages incurred due to the company's careless or dishonest trading in breach of section 22.<sup>182</sup> Even though section 22 prohibits the "company" rather than the directors, sections of the 2008 Act that put obligations or limits on the corporation may broaden the scope of directors' responsibility.<sup>183</sup>

### **3.3. The Director's Duties and Liabilities under the Existing South African 2008 Company Act**

Directors have numerous complex obligations and liabilities under the current South African Companies Act of 2008, which can be challenging to comprehend.<sup>184</sup> Directors are expected to execute their authority in a way that is best for the company and its shareholders.<sup>185</sup> They can be held accountable for failing to act in the best interests of the company and its shareholders.<sup>186</sup>

---

<sup>178</sup> Yeats (n 198)

<sup>179</sup> CDH (n 187)

<sup>180</sup> Muswaka (n 195)

<sup>181</sup> CDH (n 187)

<sup>182</sup> Ibid

<sup>183</sup> Muswaka (n 195)

<sup>184</sup> Ashirah Bibi Kaudeer, 'Does the role and duties of the business rescue practitioner as conferred by the South African Companies Act 71 of 2008 give rise to conflicts concerning the powers and duties of directors during business rescue proceedings?' (MS thesis. University of Cape Town, 2016) < <https://rb.gy/hdzzoz> > accessed on 25 April 2024

<sup>185</sup> Ibid

<sup>186</sup> Safia Mohiudeen, , 'The effect of the partial codification of the common law duties of directors in the companies Act 71 of 2008 on the liability of directors' (2018) < <https://rb.gy/o5yoak> > accessed in 25 April 2024

This section provides an overview of the duties and liabilities of directors under the South African Company Act, discussing common mistakes and inadequacies that can arise if directors fail to fulfil their obligations effectively.<sup>187</sup>

### **3.3.1 Duties of directors under the 2008 company Act**

The South African corporate law framework has codified fiduciary duties of directors and the obligation to use reasonable care and skill in a statute, a significant innovation, but not a complete or self-contained code.<sup>188</sup> This partial codification of directors' fiduciary duties was intended to prevent forcing directors to search through difficult-to-access court decisions for these obligations and to make it easy for directors to become aware of and access their fiduciary obligations.<sup>189</sup> The Directors manage the company's day-to-day operations. Shareholders select them to represent their interests. They must operate in the best interest of the company and its shareholders. They must also comply with the corporate charter and any other applicable legislation.<sup>190</sup>

Along with a fiduciary duty to act in the best interests of the company, directors have a general obligation to act honestly and in good faith. Directors must also apply their authority in ways that they believe would most successfully advance the organization's goals.<sup>191</sup> Directors must act in the best interests of their company; thus, the Companies Act contains provisions addressing directors' obligations that are like the responsibilities of directors under common law.<sup>192</sup> Section 76 of the Companies Act outlines the requirements for directors' behaviour. Section 76(3) states that "[A] director of a company, when acting in that capacity, must exercise the powers and perform the functions of director."

#### **A. A Duty to Act in Good Faith toward the Company under the Act**

King II stipulates that directors shall exercise utmost good faith, honesty, and integrity in their interactions with the company.<sup>193</sup> They must also operate independently. A person exercising

---

<sup>187</sup> Ibid

<sup>188</sup> Cassim (n 31) 507

<sup>189</sup> Mohiudeen (n 209)

<sup>190</sup> Ibid

<sup>191</sup> Ibid

<sup>192</sup> Section 76 of the Companies Act 71 of 2008

<sup>193</sup> Faatima Seedat, 'Section 76 of the Companies Act 71 of 2008 as a mechanism of enforcement for the King IV Code on corporate governance for South Africa.' (This dissertation is submitted in fulfilment of the requirements for the degree of Master of Laws, UNIVERSITY OF KWAZULU-NATAL 2019) < <https://rb.gy/ohcauq> > accessed in 25 April 2024

their rights and performing their duties as a corporate director must do so in good faith and with proper consideration for others.<sup>194</sup> Thus, Section 76(3)(a) includes two common law obligations: the duty to act in good faith and the obligation to act with purpose. The basic responsibility of a director is to use his authority and perform his duties honestly and in the best interests of the company. This responsibility supersedes all other duties and qualifies the director's other skills.<sup>195</sup> In addition, in *Re Smith & Fawcett Ltd* the court put down the long-standing and often mentioned legal concept that the directors are required to utilize the powers conferred upon them *bona fide* in what they deem not what a court may consider to be in the interests of the company.<sup>196</sup> A director thus has to behave in what he or she, in good faith, honestly believes to be in the best interests of the company.

The obligation of good faith is the main and most fundamental fiduciary duty owed by directors, and all other fiduciary obligations are derived from it.<sup>197</sup> According to Section 76, a director's *bona fide* judgment must be supported by logic.<sup>198</sup> Corporate managers must sincerely believe that their actions are in the best interests of the company, that the claims they make are true, and that they are acting in good faith. This demands good faith, which entails personal honesty, and sincerity.<sup>199</sup> Faithfulness to duties and obligations and fidelity to the office are necessary for acting in good faith and meeting the shareholders' reasonable expectations.<sup>200</sup>

## **B. The Duty to Act in the Best Interests of the Company under the Act**

The common-law principle that a director must act in the best interests of the company is codified in Section 76(3)(b) of the Act, which states that a director of a company when acting in that capacity, must exercise the powers and perform the tasks of the director in the best interests of the business.<sup>201</sup> The wording of the clause clarifies any doubts about the directors' duties to the company and the company alone. Thus, the duties can only be enforced by the firm. In

---

<sup>194</sup> Ibid

<sup>195</sup> Ibid

<sup>196</sup> Heath, P. In *Re Smith Vs Fawcett Ltd* Lord Green MR said: 2.' < <https://rb.gy/9cfpad> > accessed in 15 august 2022

<sup>197</sup> Cassim (n 31) 523

<sup>198</sup> *Visser Citrus (Pty) Ltd v Goede Hoop Citrus (Pty) Ltd and Others* 2014 5 SA at 75-76

<sup>199</sup> Melvin A. Eisenberg, 'The Duty of Good Faith in American Corporate Law.' (2006) ECFR 1-44 < <https://rb.gy/uhz6kk> > accessed in 15 august 2022

<sup>200</sup> Ibid

<sup>201</sup> Seedat (210) 37

Greenhalgh v. Arderne Cinemas Ltd., the court decided that "company as a whole" did not apply to a business operating independently of the incorporators.<sup>202</sup> It refers to a collective body of shareholders or incorporators. Aside from some extraordinary circumstances, directors are not obligated to any specific shareholder. The entire group of shareholders is the recipient of the obligation.<sup>203</sup> As a result, it is widely understood that the directors have a duty to the "company" as a whole, which refers to the full body of shareholders, including potential shareholders.<sup>204</sup> In this sense, the term "company" refers to the firm's shareholders. The same notion can also be phrased as follows: Directors must act in the best interests of current shareholders, considering both present and future interests.<sup>205</sup> The mention of future shareholders emphasizes the importance of directors considering long-term concerns rather than committing exclusively to short-term ones.

### **C. The Duty to Avoid Conflicts of Interest**

According to King II, there may be conflicts of interest arising from transactions between the corporation and its directors, management, or key shareholders.<sup>206</sup> Directors should also avoid these conflicts and refrain from placing their interests ahead of those of the company and its shareholders.<sup>207</sup> Furthermore, such conflicts should be disclosed as quickly as possible. Directors must keep all information obtained while serving in that capacity confidential and may not disclose it to anyone else without the company's permission.<sup>208</sup> This principle is repeated in Sections 75 and 76(2)(a). As a result, the director must disclose his or her financial interests, defined as "direct material interests of that person, of a financial, monetary or economic nature, or to which a monetary value may be attributed" under Section 75 of the 2008 Act.<sup>209</sup> Section 75 applies to all directors, including members of board and audit committees, as specified in the 2008 Act.<sup>210</sup> Section 75(5) requires directors to disclose their financial interests and all relevant facts if they have a personal financial stake in the outcome of an issue discussed at a board

---

<sup>202</sup> Ibid

<sup>203</sup> Ibid

<sup>204</sup> Cassim (n 21) 619

<sup>205</sup> Ibid

<sup>206</sup> King Committee on Corporate Governance, and Institute of Directors (South Africa). *King Report on Corporate Governance for South Africa* (King II Institute of Directors in Southern Africa, 2002.) 47, 55

<sup>207</sup> Ibid

<sup>208</sup> Ibid

<sup>209</sup> Section 75(1) of the Companies Act 71 of 2008

<sup>210</sup> Ibid

meeting or know someone who does.<sup>211</sup> Unless ordered or instructed by the board, the director must resign from the meeting and refuse to sign any documents about the current issue.<sup>212</sup> Any agreement or resolution adopted by the board that does not include such disclosure is null and void. It is not enforceable unless it is validated under section 75(7) by an ordinary decision or a court order under section 75(8).<sup>213</sup>

Section 76(2)(a) prohibits a director from intentionally harming the company or one of its subsidiaries by using his position as a director or information obtained in that capacity for personal advantage or the benefit of others.<sup>214</sup> This duty covers both potential disputes and actual conflicts.<sup>215</sup> The "no profit" rules from common law are reflected in this section.<sup>216</sup> *Bona fides* should not be utilized for deciding whether a conflict would have been adequately anticipated; instead, a "common sense" approach should be used.<sup>217</sup> The common law "no profit rule" is founded on the premise that utilizing someone with whom you have built a trusting and confident relationship for personal advantage is prohibited.<sup>218</sup>

#### **D. The Duty of Care, Skill, and Diligence**

According to King II, all directors, whether executive or non-executive, are responsible for exerting the level of care, skill, diligence, and diligence that can be expected of someone in their position.<sup>219</sup> To perform their duties successfully, directors have a duty of care and skill to ensure that they are well-informed about the company's operations and how they affect the economy.<sup>220</sup> A director is required by Section 76(3)(c) of the 2008 Act to carry out their responsibilities with

---

<sup>211</sup> Section 75(5) of the Companies Act 71 of 2008

<sup>212</sup> Ibid

<sup>213</sup> Ibid section 75 (7) and 75(8)

<sup>214</sup> Ibid Section 76(2)(a)

<sup>215</sup> Phillips v Fieldstone Africa (Pty) Ltd and Another 2004 (3) SA 465 (SCA) 31 <<https://rb.gy/02kyj5>> accessed in 15 august 2022

<sup>216</sup> Regal Hastings v Gulliver 1942 [1] A11 ER 378; Da Silva and Others v Ch Chemicals (Pty) Ltd 2008 (6) SA 620 (SCA). (As cited in Seedat (210) 39)

<sup>217</sup> M Havenga 'Directors exploitation of Corporate Opportunities and the Companies Act 71 of 2008' (2013) 2 TSAR at 257-268 citing Boardman v Phipps 1967 (2) AC 46, 1966 [3] A11 ER 721 (HL) at page 33(As cited in Seedat (210) 39)

<sup>218</sup> Seedat (210) 37

<sup>219</sup> King II (n 226) 54

<sup>220</sup> Ibid

the degree of care, skill, and diligence that would be expected of someone with the breadth of knowledge, expertise, and experience that the director possesses.<sup>221</sup>

When someone operating in a fiduciary role for another person does so for their gain or at the expense of the other, that person has violated their trust.<sup>222</sup> Since it develops independently of contract or delict, the cause of action for a breach of fiduciary obligation is *sui generis*.<sup>223</sup> The complaint stems from a violation of trust. However, the ground of action for a breach of the duty of care is based on delict, which requires the proving of wrongfulness, culpability, the loss experienced, and causation for the corporation to recover damages.<sup>224</sup>

### 3.3.2 Liability of directors under the 2008 company Act

Sections 77(1)–(10) establish the liability of a company's directors and prescribed officers, and this section also applies to alternate directors, audit committee members, and board committee members, regardless of whether they are also members of the company's board of directors.<sup>225</sup> Section 218(2) of the Act adds Section 77 by saying that anybody who violates any Act's provisions is liable to anyone else for any loss or harm resulting from that violation. Section 218(2) purposefully uses the term "any" twice to emphasize the vast scope of its application.<sup>226</sup> Furthermore, unless this is ratified by special resolution, each shareholder of a company has a claim for damages against any person who, in breach of section 20(6), causes the company to act in contradiction to the Act or any limitation, restriction, or qualification on the company's purposes, powers, or activities (or a limitation on the directors' authority).<sup>227</sup> Section 78(2) nullifies any clause that directly or indirectly attempts to exempt a director from the obligations mentioned in Section 77.<sup>228</sup> This includes clauses from the company's bylaws, memorandum of incorporation, agreements, and resolutions. This cannot be used to reduce or remove the director's liability.<sup>229</sup> On the other hand, section 77(9) allows the court the power to release a

---

<sup>221</sup> Section 76(3)(c) of the Companies Act 71 of 2008

<sup>222</sup> *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 < <https://rb.gy/gi0qdw> > accessed in 26 April 2024

<sup>223</sup> *Ibid*

<sup>224</sup> E. Jones, 'Directors' duties: negligence and the business judgment rule.' (2007) SA Mercantile Law Journal 326-336.< <https://rb.gy/jnyn7s> > 26 April 2024

<sup>225</sup> Section 77(1) of the Companies Act 71 of 2008

<sup>226</sup> 218(2) of the Companies Act 71 of 2008

<sup>227</sup> Section of 20 of the Companies Act 71 of 2008

<sup>228</sup> *Ibid* section 78(2)

<sup>229</sup> Cassim (n 31) 583

director from liability for conduct that is not deliberate misconduct or an intentional breach of trust if the director acted honestly and reasonably or deserved somewhat to be released from liability.<sup>230</sup>

Section 77(6) states that a person's culpability for the same Act is joint and several with that of another.<sup>231</sup> A three-year prescription period applies to actions to recover any loss, damages, or expenses for which a person is or may be held liable under section 77 (section 77(7)).<sup>232</sup> According to Section 77(8), until the procedures are abandoned or such a person is exonerated, a person liable under Section 77 is equally and separately obliged to pay the expenditures of all the parties in court actions to enforce liability under Section 77.<sup>233</sup> This includes reimbursing the corporation for any money paid mistakenly as a result of the contested Act but not eligible for reimbursement under the Act.<sup>234</sup> Sections 77(2) through (5) define the liabilities of a company's directors. As explained in the next section.

#### **A. Breach of fiduciary duty**

Under the common law principles related to breach of fiduciary duty (duty to act in good faith and the best interests of the company), a director may be held liable for any loss, damages, or expenses incurred by the company as a result of a breach by a director of a duty envisioned in Section 75 (disclosure of a director's financial interests), Section 76(2) (improper use of position or corporate information and failure to communicate relevant information to the company), or Section 76(3)(a) or (b).<sup>235</sup>

The common law fiduciary duties and the statute are connected by section 77(2)(a). However, the problem with this particular clause is that it only addresses liability for "any loss, damages, or costs sustained by a company," leaving unaddressed the restitution of profits a director earns in contravention of the no-profit rule—which is applicable even in situations where the profit is not made at the company's expense.<sup>236</sup> This is demonstrated by the facts of the landmark case of

---

<sup>230</sup> Section 77(9) of the Companies Act 71 of 2008

<sup>231</sup> Ibid section 77(6)

<sup>232</sup> Ibid section 77(7)

<sup>233</sup> Ibid section 77(8)

<sup>234</sup> Cassim (n 31) 583

<sup>235</sup> Section 77(2)(a) of the Companies Act 71 of 2008

<sup>236</sup> Cassim (n 31) 584

Regal (Hastings) Ltd v. Gulliver, in which directors were required to disgorge gains obtained even though the company did not suffer a loss and would have profited from their actions.<sup>237</sup>

### **B. Breach of the duty of care and skill or other provisions**

Section 77(2)(b) holds a director responsible for any losses, expenses, or damages incurred by the company due to the director's breach of duty as per Section 76(3)(c) (failure to exercise reasonable care, skill, and diligence). This upholds the traditional common-law principles by imposing liability for negligence in breaching the director's duty of care and skill. This applies to any provision of the Act not otherwise listed in section 77, or any provision of the company's Memorandum of Incorporation.<sup>238</sup>

The obligations mentioned in Section 77(2)(a) and (b) are owed to the corporation rather than the company's shareholders.<sup>239</sup> Under these laws, it is the company's responsibility to act against the dishonest director. If a shareholder (or another interested party) wishes to seek compensation for these corporate wrongs, he or she must do so by launching a derivative action, not a personal action, or by relying on Section 218. (2).<sup>240</sup> Liability under section 77(3) describes the circumstances in which a director may be held liable for losses, expenses, or damages incurred by the corporation as a direct or indirect consequence of any of the following: Acted in the company's name, signed anything in the company's name, or attempted to bind or authorize actions on its behalf despite lack of authority, conducted business dishonestly or carelessly with gross negligence in violation of section 22. (1) participated in a company act or omission with the intent to mislead creditors, employees, or shareholders, or for another fraudulent purpose, authorized the publication of materially false or misleading financial statements, prospectuses, or written statements containing "untrue statements" or false statements about director consent. Under Section 77(3)(e), a company's director is additionally accountable for any losses, expenses, or costs incurred by the company as a direct or indirect result of the director's

---

<sup>237</sup> Ibid

<sup>238</sup> Ibid Section 77(2)(b) of the Companies Act 71 of 2008

<sup>239</sup> Cassim (n 31) 585

<sup>240</sup> Ibid

attendance at a meeting or decision-making outside of a meeting (under Section 74) and failure to vote.<sup>241</sup>

A director will only be held liable for failing to vote against a distribution that breaches section 46 under section 77(4) if the distribution causes the firm to fail the solvency and liquidity tests. Furthermore, it must have been reasonable to expect that the firm would pass the solvency and liquidity conditions before the distribution vote was held.<sup>242</sup>

Section 77(4)(b) states that a director's liability under this section is limited to the total distinction between the amount that the company was able to recover from the amount distributed to the recipients and the total by which the distribution's value exceeded the amount that would have been distributed without making the company fail the solvency and liquidity test.<sup>243</sup>

### **3.4 The United Kingdom Company Law: An Overview**

The contemporary form of company law in the UK originated in the middle of the nineteenth century, though previous business alliances existed.<sup>244</sup> The history of modern company law in England began in 1844 when the Joint Stock Companies Act was passed. The Act provided for the first time that a company could be incorporated by registration without obtaining a Royal Charter or sanction by a special Act of Parliament. The office of the Registrar of Joint Stock Companies was also created.<sup>245</sup> During the early years of Queen Victoria's reign, corporation law in the United Kingdom underwent major changes. In 1844, the public was able to incorporate joint stock companies by registration, which was previously only possible with a charter or private Act of Parliament.

---

<sup>241</sup> Mihai Lucian Carciumaru, 'An Assessment of the Impact of Corporate Governance Codes and Legislation on Directors and Officers Liability Insurance in South Africa' (A dissertation submitted to the Faculty of Commerce, Law and Management of the University of the Witwatersrand, in fulfilment of the degree of Master of Commerce, 2009. < <https://rb.gy/2msvbq>> accessed on 29 April 2024

<sup>242</sup> Ibid

<sup>243</sup> Cassim (n 31) 586

<sup>244</sup> Turner, John D. (2017): The development of English company law before 1900, QUCEH Working Paper Series, No. 2017-01, Queen's University Centre for Economic History (QUCEH), Belfast

<sup>245</sup> Rahul Kumar Singh - 5th Year Origin and Evolution of the Modern Company Law - National Law University, Jodhpurn < <https://www.legalserviceindia.com/articles/eocindia.htm>> accessed in 30 April 2024

The 1844 Act for the Registration, Incorporation, and Regulation of Joint Stock Companies prohibited limited liability and mandated shareholder registration and audited balance sheet registration.<sup>246</sup> The Act denied to the members the facility of limited liability. The English Parliament in 1855 passed the Limited Liability Act providing for limited liability to the members of a registered company. The Limited Liability Act (18 & 19), which allowed businesses to register with limited liability, was the next big development that happened in 1855. The Joint Stock Companies Act (19 & 20) of 1856 eliminated the specific registration-related rules as well as the 1844 mandated accounting and auditing standards. From this point on, any seven individuals could create a limited liability company by each subscribing to one share. The 1862 Companies Act made no substantive modifications, but it combined the 1856 laws with other banking-related regulations.<sup>247</sup> After 1856, England's commercial law was the most permissive in Europe.<sup>248</sup> In 1900, England boasted the world's largest stock market and was the leading industrial nation. However, after 1900, the development of corporate law was primarily focused on addressing the agency issues that resulted from the conflict of behaviors, namely, shareholders versus managers, shareholders versus other constituents, creditors, and employees.<sup>249</sup>

### **3.4.1 The UK Companies Act 2006**

A major reorganization of UK company law took place in 2006. The UK Companies Act 2006 was the new company law that came into effect. One of the first countries to set regulations for the companies to operate was the United Kingdom. The main source of UK company law is the Companies Act 2006, an Act of the United Kingdom Parliament. With 1,300 sections, it held the distinction of being the longest in the history of the British Parliament.<sup>250</sup> The Act offers a comprehensive code of company law for the United Kingdom and made reforms to practically every aspect of the law relating to firms.<sup>251</sup> One of the Act's main features is that it codifies some common law principles that already exist, like those regarding the director's duties. Section 7 (1) of the UK Companies Act 2006 states the basis by which a company is incorporated and

---

<sup>246</sup> Josephine Maltby (1998) UK joint stock companies legislation 1844-1900: accounting publicity and "mercantile caution" accessed in 1 may 2024

<sup>247</sup> Ibid

<sup>248</sup> Ibid

<sup>249</sup> Ibid(n.272)

<sup>250</sup> Dr. Rajesh Kumar Agrawal (2015) A COMPARATIVE STUDY OF UK COMPANIES ACT, 2006 AND INDIAN COMPANIES ACT, 2013 *Volume : 1(4)* 33-36

<sup>251</sup> Ibid

becomes a separate legal entity from its owner. Providing all the required documentation to the Registrar of Companies completes the registration process.<sup>252</sup>

Directors are the individuals who oversee running the business and make choices on how to run it daily for the benefit of the shareholders. Despite not being formally appointed as a director, the UK Companies Act, of 2006 allows for a special kind of director known as a Shadow Director, who either manages the company's management or acts on the directors' orders. Section 152 of the UK Companies Act, 2006 states that a public company must have at least two directors, and a private company must have at least one director. There is no legislative maximum number of directors.<sup>253</sup> The Companies Act of 2006 established a legal requirement for a business review in the director's report. The statute requires companies to promote their success for the benefit of all shareholders. Companies must include a business review in their annual directors' report, allowing shareholders to assess directors' performance under section 172 of the Companies Act.<sup>254</sup>

### **3.4. The Director's Duties and Liabilities under the existing UK 2006 Company Act**

The section (sections 232 to 239) of the UK Companies Act 2006 deals with Directors' Liabilities, the removal of criminal liability on the part of the company for failures to comply with the requirements of section 237 and the acts giving rise to liability on the part of a director (section 239).<sup>255</sup>

#### **3.4.1 Duties of directors under the 2006 company Act**

Under English company law, directors have historically been subject to duties. However, until recently, case law had evolved to establish the great bulk of directors' duties rather than being explicitly stated in legislation.<sup>256</sup> Section 172 of the Act outlines this duty and provides that a director must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole.<sup>257</sup> This resembles the existing common law need to behave in the business's "best interests" significantly. But the section also

---

<sup>252</sup> Section 7 of the UK company act 7(1) 2006

<sup>253</sup> Ibid(n.278)

<sup>254</sup> Section 172 of the company act 2006

<sup>255</sup> Companies Act 2006 section 232,239

<sup>256</sup> Scott Leonard and David Webster (2009) Overview of Directors' Duties under the Companies Act 2006 accessed in 1 may 2024

<sup>257</sup> Section 172 of the company act 2006

lays out a list of non-exhaustive elements that a director needs to take into account when determining what would likely promote the success of the company.

### **A. Duty of Skill and Care under the Company Act**

A director is required to act with the care, skill, and diligence that a reasonably diligent person would exercise if they had both (i) the general knowledge, skill, and experience that is expected of a director and (ii) their general knowledge, skill, and experience. This duty of skill and care places the existing negligence law on a statutory footing.<sup>258</sup> Stated differently, every director will be subject to the criteria of a “reasonable director” and be presumed to possess the knowledge, skills, and experience typical of a director in that capacity. Furthermore, a director possessing supplementary or advanced expertise, such as qualifications in accountancy, will be held to the same standards as a responsible director possessing this kind of knowledge.<sup>259</sup>

### **B. Duty to Declare Interests**

The nature and extent of any interest a director may have in any transaction or arrangement in which the company is or may be a party must be disclosed to the board of the company. There are two sections: section 177, which deals with a declaration made before the transaction or arrangement, and section 182, which deals with a declaration made about an agreement or transaction in which the company has already participated.<sup>260</sup> It means a director is required to disclose their interest if they are aware of it before the arrangement is made. However, a director is required to declare as quickly as possible if they only learn of their interest or if the interest only arises after the firm has engaged in the arrangement. Therefore, if a director does not know about their interest in the transaction or arrangement that the company is a party to, there is no violation of these duties. Furthermore, a director is exempt from disclosing an interest if they are not aware of a potential conflict or if it is not reasonable to assume that their interest will result in a conflict.

---

<sup>258</sup> Section 174 of the company act 2006

<sup>259</sup> Ibid (n.284)

<sup>260</sup> Section 177 and 182 of the company act 2006

### **C. Duty to Avoid Conflicts**

A director must stay out of any circumstance in which their interests or those of the company could conflict, either directly or indirectly. This duty specifically applies to a director exploiting any property, information, or opportunity.<sup>261</sup> Transactions or agreements with the corporation are exempt from this responsibility; there will be no violation if it is not reasonably foreseeable that the circumstances will result in a conflict of interest.<sup>262</sup>

### **D. Other Duties under the Companies Act 2006**

Directors must operate within the scope of their authority granted by the company's charter and for the right reasons (section 171) of the act and required to use independent judgment (section 173), but this does not stop a director from acting in line with a contract to which the company is party (i.e., the section acknowledges that directors will not have total freedom to act in the company's best interests because the company will be bound by various contractual obligations), and a director may act in line with the company's charter. and A director is not permitted to receive gifts or other inducements from outside parties as a result of his role as a director or as a means of persuading him to act in a particular manner (section 176). If the gift or enticement cannot rightly be viewed as creating a conflict of interest or if it amounts to money for services rendered to the business, there won't be a breach.<sup>263</sup> General Duties of Directors are outlined in Sections 170 to 181 of the act. As stated in the current legislation, Section 170(1) specifies that a director owes the general duty to the company. Thus, they can only be enforced by the firm, just like they are now. Members' derivative claims and actions are covered in Part 11, which outlines the process by which they can enforce the company's obligations<sup>264</sup>.

#### **3.4.2 Liability of directors under the 2006 UK Company Act**

A director's duties are owed to the corporation, not third parties. In some cases, directors may assume personal liability to third parties, either explicitly or implicitly. By personally guaranteeing the firm's obligations, a director could explicitly assume personal liability, usually to a landlord, bank, or finance company. Additionally, there are circumstances in which a

---

<sup>261</sup> Ibid (n.284)

<sup>262</sup> Section 175 of the company act 2006

<sup>263</sup> Section 171,173,176 of the company act 2006

<sup>264</sup> Section 170 to 181 of the company act 2006

director may implicitly take on personal liability. *Williams and Others v. Natural Life Health Foods Ltd. and Others*, *The Times*, January 9, 1997, is the top case. Based on personal experience, a franchisor firm director provided false advice to a franchisee, possibly unrelated to his role as a director. Initially, the Court of Appeal determined that the director owed the client who had relied on the advice personally. Though these scenarios are uncommon, the House of Lords reversed the ruling, stating that personal culpability would only be applied in extreme cases.<sup>265</sup> The director who signed a contract was found to have made an implicit claim about the company's solvency to a supplier, which he knew to be false, in the *Context Drouzhba Ltd v. Wiseman and Anor* [2006] EWHC 2708 (QB) case. The supplier held the director personally liable for misleading.<sup>266</sup> A director's responsibilities are to the company, not to specific shareholders. In the event of a duty breach, shareholders lack a clear cause of action against directors. A firm can find itself unable or unwilling to file a lawsuit against a current or former director.<sup>267</sup> Court procedures initiated by shareholders in the company's name against a director (or other third party) for negligence, violation of duty, or breach of trust are referred to as derivative actions or claims.<sup>268</sup>

The Act's Section 178 outlines the consequences of breach, stating that it maintains the current civil penalties for violating or threatening to violate any of the general duties. The remedies available for a breach of the common law norms and equitable principles that the general responsibilities replace will be precisely the same if the general duties are violated. The duties are enforceable in the same manner as any other fiduciary duty due to a corporation by its directors, as stated in subsection (2) of this section (except the need to exercise reasonable care, skill, and diligence, which is not regarded as a fiduciary duty). The following are possible outcomes of a breach of fiduciary duties:

- damages or compensation where the company has suffered a loss;
- restoration of the company's property;
- an account of profits made by the director; and

---

<sup>265</sup> *Ibid* (n.284)

<sup>266</sup> *Ibid* (n.284)

<sup>267</sup> Section 260 of company act 2006

<sup>268</sup> Section 264 of company act 2006

- rescission of a contract where the director failed to disclose an interest.<sup>269</sup>

### 3.5 The German Company Law: An Overview

Given Germany's dominance, the history of German corporation law is primarily preserved in the German language. Germany, as a prominent European power, has had a significant impact on the development of European Union (EU) business law. Historically, it has also played a major role in shaping Western legal study in the early 20th century. In response to the demands of war capitalism, economic and political crises, and the Nazi takeover of power in 1933 (Machtergreifung), German practice diverged substantially from other capitalist systems to establish a distinct corporate law system.<sup>270</sup> After World War II, German company law has been evolving within a globalized framework. The revival of liberal ideas, the Allied occupation, and West Germany's desire to reintegrate into the Western capitalist system have led to changes in German corporate law. This has made convergence challenging, particularly about the two-tier board structure and its connection to co-determination.<sup>271</sup>

The Railway Corporations Law was the first Prussian regulation governing the formation and functioning of corporations in 1838. This law established general operating requirements for railway businesses, even though they still needed a concession to incorporate. This is the first attempt by the German government to put corporate governance on a contemporary, normative legal footing.<sup>272</sup> And followed in 1843 by Prussia's first universal corporate legislation. The French Code de Commerce and the Dutch Commercial Code of 1838 served as the main sources for the 1843 law, which allowed limited liability but only joint stock companies.<sup>273</sup> In the Establishment of Modern Corporation Law, it is stated that the 1870 law allowed for the creation of a company through registration, featured several formalities and limits on the formation of companies, and prohibited the distribution of dividends in situations where doing so would reduce the company's capital. A prohibition on the company transactions in its shares, a restriction on supervisory and management board members transacting with the firm unless

---

<sup>269</sup> Section 178 of company act 2006

<sup>270</sup> Muchlinski P. The Development of German Corporate Law Until 1990: An Historical Reappraisal. *German Law Journal*. 2013;14(2):339-379. doi:10.1017/S2071832200001838

<sup>271</sup> Ibid

<sup>272</sup> Ibid

<sup>273</sup> Ibid

approved by a two-thirds majority at the general meeting, and new accounting regulations and criminal penalties<sup>274</sup>

### 3.5.1 The German Corporate Governance of Stock Corporations

German law recognizes two kinds of business corporations, the Aktiengesellschaft (Stock Corporation-AG) and the Gesellschaft mit beschränkter Haftung (Company with Limited Liability-GmbH).<sup>275</sup> In comparison to an AG, a GmbH is easier to run and less expensive; it also gives incorporators greater control over the relative responsibilities and rights of officers and shareholders and does not demand the release of financial statements.<sup>276</sup> Initially, the German Commercial Code (Handelsgesetzbuch-HGB) regulated the AG. The Aktiengesetz (Stock company Law), a special company statute, was passed in 1937 and addressed it. The 1937 Aktiengesetz was criticized for favouring management at the disadvantage of shareholders following World War II and the rise of a free market economy.<sup>277</sup> As a result, the new Aktiengesetz (AktG), which went into force on January 1, 1966, is enacted. The new regulation aims to strengthen the position of shareholders by specifically making corporate shares more appealing to the general public as an investment.<sup>278</sup>

Due to the strong discussion on corporate governance in Germany, the stock corporation has emerged as the most important entity in company law. Business judgment rule will finally be included as a general principle applicable to directors' duties and liabilities under AktG with the new Gesetz zur Unternehmensintegrität und Modernisierung des Aktiengesetzes Law on Company's Integrity and on the Modernization of the Stock Corporations Act), which was expected to come into force by the end of 2005.<sup>279</sup> AktG will eventually incorporate the business judgment rule as a basic guideline that applies to directors' duties and liabilities. The primary focus of the reform was on the mandatory two-tier board model, which is the cornerstone of internal corporate governance in German stock companies. All German stock companies, regardless of size or listing, are required to establish a supervisory board to oversee and counsel

---

<sup>274</sup> Ibid

<sup>275</sup> Ernest C. Steefel and Bernard von Falkenhausen, New German Stock Corporation Law, 52 Cornell L. Rev. 518 (1967) Available at: <<http://scholarship.law.cornell.edu/clr/vol52/iss4/2>> accessed in may 7 2024

<sup>276</sup> Ibid

<sup>277</sup> Ibid

<sup>278</sup> Ibid

<sup>279</sup> Leyens PC. German Company Law: Recent Developments and Future Challenges. German Law Journal. 2005;6(10):1407-1417. doi:10.1017/S2071832200014395

the management board.<sup>280</sup> The Supervisory Board's control powers were reinforced when the 1998 reform assigned it the responsibility of concluding the auditing contract and deciding the auditing process's focal point. The changes also addressed the conflicts of interest that resulted from the widespread use of intensive cross-directorships and bank representative mandates by limiting the quantity of supervisory roles an individual can concurrently occupy.<sup>281</sup> A governmental commission on corporate governance was appointed in 2000, two years after the current discussion on corporate governance began. The 2001 report formed the foundation for the Transparenz- und Publizitätsgesetz (TransPuG)20 of 2002 (the Law on Transparency and Disclosure), which was another significant reform of the AktG. One of the main components of the TransPuG is the annual corporate governance statement.<sup>282</sup> Under a draft Gesetz zur Verbesserung der Haftung für falsche Kapitalmarktinformation (KapInHaG) (Capital Market Information Liability Act), the most recent reform project aimed to significantly increase the personal liabilities of management and supervisory board directors for breaches of information duties. One of its main flaws was the absence of a system to shield directors from retaliatory shareholder actions and to shield the business from the risk that management would spend more time in court than running the business.<sup>283</sup>

### **3.5.2 The Director's Duties and Liabilities under the existing Germany Company law**

Members of the management board are supposed to put in a significant effort to maximize profits and guarantee a business's profitability. In the process, they have to make judgments that are frequently dangerous and in circumstances where the results of such decisions cannot be foreseen with certainty.<sup>284</sup> Such high-risk choices could result in gains for the business as well as losses. Clear norms of procedure are necessary to safeguard the interests of those connected to a company and provide board members with an adequate degree of freedom of action.<sup>285</sup> It is important that owners and management board members have direction from the legislation and case law regarding when board actions are appropriate and when they may put them in danger. the duties, rather than the details of a director's responsibilities, a board member's behavior

---

<sup>280</sup> Ibid

<sup>281</sup> Ibid

<sup>282</sup> Ibid

<sup>283</sup> Ibid

<sup>284</sup> KARIN MADISSON (2012) Duties and liabilities of company directors under German and Estonian law: a comparative analysis”, RGS Research papers, No. 7, 2012, pp. 1-80, p. 1.

<sup>285</sup> Ibid

should be determined by their degree of concern, knowledge, and understanding. The duty of care and the obligation of loyalty are these guiding concepts.<sup>286</sup> German law appears to have a wider and advanced range of fiduciary duties than other legal systems due to the existence of a business judgment rule that limits board members' liability, allowing them to take reasonable risks and foster business growth without worrying about losing their personal assets in the event of a failure.<sup>287</sup> A company's management board members are not held personally liable for the actions of the company, but a company is liable for the performance of its obligations with all of its assets. In the event that a member of the management board fails their duties, they could face personal liability in front of the company's creditors, shareholders, or other stakeholders. A management board member may, in this case, be subject to two different kinds of obligation: external liability and internal liability toward the company and third parties, respectively.<sup>288</sup>

### 3.5.3 The Duties of directors under Germany Company Law

The duties focus on the degree of skills, knowledge, and care. This principle is “Already in the ancient Rome, the principal of *"bonus pater familia"* a.k.a. "the good family father" was required to be followed whenever acting on behalf of another. By analogy, the member of the managing body is obligated to show the care for the matters of the business entity in the same manner as a father care for his wife and children”<sup>289</sup> The concept of loyalty is an important part of ethics. A general duty to behave with the diligence of a responsible businessperson rests on each director. In carrying out their duties, directors must adhere to all applicable laws, the statutes and articles of association of the company, any directives given at shareholder meetings, and the terms of their employment agreements.<sup>290</sup> Directors are not permitted to make any payments after the firm declares bankruptcy unless they are consistent with the diligence of a competent businessperson in any case. Payments made in the regular course of business throughout the allowed insolvency filing time are considered to have been paid with the prudence of a prudent businessperson, so long as the directors pursue the bankruptcy file or work toward resolving the insolvency.<sup>291</sup>

---

<sup>286</sup> Ibid

<sup>287</sup> Ibid

<sup>288</sup> Ibid

<sup>289</sup> Ibid

<sup>290</sup> Andreas Lehmann (2023) Directors' Duties – Germany Considerations for Directors When a Company Is in Financial Difficulty [squirepattonboggs.com <https://eu.docworkspace.com/d/sINaPmKP\\_Ac-TjBjG>](https://eu.docworkspace.com/d/sINaPmKP_Ac-TjBjG) accessed in 4 may 2024

<sup>291</sup> Ibid

## **A. Duty of care and duty of loyalty**

### **i) Duty of care**

The duty of care principle states that each member of the directors is responsible for managing the organization in the best interests of the company and with the diligence that is typically anticipated of someone in their position. To increase the enterprise's sustainable value, the director must act in the best interests of the business.<sup>292</sup> It is imperative for the directors to ensure that the terms and conditions of any agreements they enter with shareholders comply with normal market standards. The directors are responsible for carrying out their management duties with due care, and they are liable to the corporation jointly and severally for any damages that arise from their failure to do so.<sup>293</sup> When in doubt, it is the responsibility of the involved directors to demonstrate that they took the appropriate care in the given situation.<sup>294</sup> A director is required to handle all company-related affairs with the diligence of a prudent businessman. The managers are required to run the business with the same level of caution that one might anticipate from a regular, wise businessman. Directors are obliged to use all caution that can be taken, but much more than one might anticipate from a regular man.<sup>295</sup>

### **ii) Duty of loyalty**

The duty of loyalty is the obligation to protect the interests of the company. This is based on concrete obligations, including exercising powers for their intended purposes, refraining from pursuing personal business opportunities related to the corporation's existing or planned business, and refraining from engaging in trades or transactions in the company's line of business on their own or on behalf of others. In Germany, self-contracting and multiple representations are prohibited.

The Civil Code prohibits agents from entering transactions on behalf of their principal, either in their own name or as agents for a third party, unless the transaction is solely for the fulfilment of an obligation. A director cannot represent the company in negotiations with themselves or a third

---

<sup>292</sup> Ibid (n.308)

<sup>293</sup> Stock Corporation Act 93

<sup>294</sup> Stock Corporation Act 93(2)

<sup>295</sup> Ibid(n.312)

party they represent<sup>296</sup> The duty of loyalty also includes the board member's duty of confidentiality.<sup>297</sup> A director is required by law not to compete with the company's business while in office, regardless of whether the covenant is specifically stated in the service contract, articles of organization, or by legislation.<sup>298</sup>

## **B. Duties of directors When a Company is in Financial Difficulty**

- i. Directors have a duty to keep an eye out for events that can harm the company's survival and to act appropriately to avoid them.
- ii. German insolvency law places obligations on directors in cases of insolvency or impending insolvency that are intended to safeguard the interests of the company's creditors. Among these obligations is the need to promptly file for insolvency.
- iii. Directors must file for bankruptcy as soon as possible and, at the latest, either (i) within three weeks of the company's inability to pay its debts on time (apart from a brief and minor liquidity shortage) (illiquidity); or (ii) within six weeks of the company's becoming overly indebted and having a poor prognosis for continuing as a going concern.
- iv. Directors are not permitted to make any payments after the company declares bankruptcy unless they are consistent with the diligence of a competent businessperson in any case. Payments made in the regular course of business throughout the allowed insolvency filing time are considered to have been paid with the prudence of a prudent businessperson, so long as the directors pursue the bankruptcy file or work toward resolving the insolvency.
- v. Directors are required to uphold the rights and interests of the company's creditors in the event that the business starts restructuring procedures in accordance with the recently enacted restructuring rules (shift of fiduciary obligations).<sup>299</sup>

### **3.5.4 Liability of directors under the German Stock Corporation Act**

Corporate governance laws in Germany are included in several legal codes. The German Commercial Code (Handelsgesetzbuch HGB), the German Civil Code (Bürgerliches Gesetzbuch BGB), the Private Limited Companies Act (Gesetz über die Gesellschaft mit beschränkter Haftung GmbHG), and the Stock Corporation Act (Aktiengesetz AktG) are the most important

---

<sup>296</sup> Ibid (n.312)

<sup>297</sup> Section 93 of the German stock corporate act

<sup>298</sup> Ibid (n.312)

<sup>299</sup> Ibid (n.318)

ones.<sup>300</sup> directors are not held strictly liable for any losses incurred by the business or its creditors. Although ineffective management will eventually hurt the business, it won't always result in personal culpability for potential losses. Directors who wilfully breach their obligations may be held personally liable. Such obligations may arise from the legislation (civil, corporate, criminal, or insolvency law) or from a contract (articles of organization, contract with the director, etc.).<sup>301</sup> German law distinguishes between internal liability to the company and external liability to third parties. Directors may also face administrative or criminal charges.<sup>302</sup>

**Internal liability** refers to a breach of duty as a director of a company. Directors are jointly and severally liable for losses incurred by failing to care for a prudent and diligent manager and rigorous management practices. The term "jointly and severally" means that each controlling director is liable for the total amount of damages.<sup>303</sup> Directors, shadow directors, and de facto directors are typically held liable like de jure directors. Directors and workers frequently follow the instructions of the majority shareholder, even if they are not technically a director or involved in the company's management. The individual may face the same liability for company damage as the **de jure directors**. In addition Members of the management or supervisory board who violate their obligations are held jointly and severally liable, including any third parties that induced them to act against the company's interests.<sup>304</sup>

**External liability** refers to all obligations owed to parties other than the company. The management board's duties are primarily to the corporation and not third parties, making external liability unusual. Typically, third-party claims for damages can only be launched against the company, with redress available against the director.<sup>305</sup> A director may be personally liable for paying applicable taxes. Payments to shareholders that violate capital maintenance regulations may result in third-party claims. They may be compelled to restore the full sum and any resulting damage.<sup>306</sup> Personal liability is only excluded if payments were made in accordance with reasonable business practices. This involves justifying each payment as required or averting additional damage to the company. If the director fails to file an insolvency petition or refrains

---

<sup>300</sup> Ibid (n.312)

<sup>301</sup> Ibid (n.312)

<sup>302</sup> Ibid (n.312)

<sup>303</sup> Ibid (n.312)

<sup>304</sup> Section 117 of Stock Corporation Act

<sup>305</sup> Sieg, O.(2022) Directors' Liability and Indemnification, *A Global Guide, Fourth Edition* pp. 119, 124

<sup>306</sup> Section 93 of Stock Corporation Act

from making payments during an insolvency scenario, they will be held liable for any losses they cause to both the company and third parties.<sup>307</sup> misinformation regarding the company's current financial situation inaccurate information during a takeover in which directors failed to appropriately manage the capital contribution collection. Under such circumstances, the directors may be sued individually by the shareholders on the basis that they breached their fiduciary duty to them.<sup>308</sup>

**The criminal liability** Failure to file for insolvency in a timely manner is a criminal offense. Directors may face imprisonment for up to three years (or one year in the case of carelessness) or a fine. Furthermore, directors will be barred from future director posts for a term of five years if convicted of failing to file for insolvency.<sup>309</sup>

**Personal (Civil) Liability** If a company suffers loss because of the directors' breach of duty, the insolvency administrator may hold them personally liable. Directors have severe liability for transactions at an undervalue or transactions detrimental to creditors unless the bankruptcy administrator can effectively claw back the appropriate funds from the receiver under applicable claw back rules. In addition, directors may be held personally liable for the following: paying debts to shareholders to the extent that doing so makes the company unable to pay its debts on time; making payments to shareholders after the company became insolvent that were not made with the diligence of a prudent businessperson even in an insolvency; failing to pay certain taxes and social security contributions; and repaying statutory share capital to shareholders in violation of statutory capital maintenance rules (including by way of upstream guarantees).<sup>310</sup> In addition to anyone else liability the members of the company's management and supervisory boards will also be held jointly and severally liable if they violated their duties. In the event of a disagreement regarding whether or not they have used the care of a diligent and conscientious management, they will be the ones with the burden of evidence.<sup>311</sup>

---

<sup>307</sup> Ibid (n.312)

<sup>308</sup> Ibid (n.333)

<sup>309</sup> Ibid (n.318)

<sup>310</sup> Ibid (n.318)

<sup>311</sup> Section 310 of German Stock Corporation Act

### **3.6 Conclusion**

Under South African, UK, and German corporate law, the duties and liabilities of directors are outlined in the Companies Act, the Stock Corporation Act, and other pieces of legislation. In charge of a company's management are directors or members of the management board, who are expected to act in the best interests of the company. They also have to take all reasonable steps to safeguard the company's assets and the directors' own when they know or should know of a possible legal breach. If the management and supervisory board members of the corporation breached their duties, they will also be held liable jointly and severally. Internal, external, criminal, and civil liabilities are all possible forms of liability.

All together, the directors owe the following duties (and liabilities) to the company: (a) to fulfil their duties as board members in good faith; (b) to confirm that they have acted in accordance with the Companies Act; (c) to carry out their duties impartially, in good faith, and with the care that a reasonably prudent person would exercise in similar circumstances; and (d) to avoid conflicts of interest. In addition, directors who breach their duties in the course of their work bear personal responsibility for any resulting losses—direct or indirect. The directors' liabilities arise from their failure to fulfil their fiduciary duties to the company as well as from their performance of their statutory obligations.

## **Chapter Four**

### **Directors' Duties and Liabilities under the Ethiopian Company Law: Lessons from South African, UK and Germany Company Law**

#### **4.1 Introduction**

This chapter mainly explores the duties and liability of directors under Ethiopia's new commercial laws and draw corporate law lessons from South Africa, the United Kingdom, and Germany. Despite the numerous changes, it is be important to evaluate the shortcomings in Ethiopian business law and consider potential lessons from the company laws of South Africa, the United Kingdom, and Germany. Finally, the chapter will conclude with recommendations after providing a summary of the primary findings of the thesis.

#### **4.2 The formulation of directors' Duties and Liabilities under the revised Ethiopian Company Law: Lessons from South African UK and German Company Law**

##### **4.2.1 Significant changes brought by the revised commercial code**

The recently established FDRE Commercial Code grants the board of directors the authority to govern a share company.<sup>312</sup> The updated Ethiopian Commercial Code allows both a share company and a private limited company to be governed by a board of directors, as opposed to the previous 1960 Ethiopian Commercial Code, which only required share firms to nominate directors.<sup>313</sup> The repealed Commercial Code required directors to be company stockholders. The new Code, which allows firms to appoint non-shareholders as directors, has repealed this restriction.<sup>314</sup> Thus, the new law incorporates the "stockholders" method, wherein only shareholders of a firm may serve on the board of directors; and the "stakeholder" approach, wherein a stakeholder who is not a shareholder may serve on the board of directors.<sup>315</sup> By enabling independent directors to serve on the board, the company will benefit from their outside

---

<sup>312</sup> Art. 296(1) of Commercial Code of Ethiopia, Proclamation No. 1243/2021

<sup>313</sup> Ibid Art. 296(4)

<sup>314</sup> Ibid Art. 296(2)

<sup>315</sup> Belete (n 140)

viewpoint and impartial vision.<sup>316</sup> The supervisory board is an additional innovation in the new Code. A company can create a supervisory board and a board of directors.<sup>317</sup>

Most importantly, the new code clearly states the obligations and liabilities of directors in addressing governance issues.<sup>318</sup> The new code includes an illustrative list of duties for directors delegated by the shareholders' general meeting and the memorandum of association.<sup>319</sup> The new Commercial Code expands board members' liability to cover personal property. It establishes stringent guidelines to protect companies, shareholders, and creditors against the faults of directors.<sup>320</sup> Any harm to the firm caused by the directors will result in civil and criminal liability unless it can be shown differently.<sup>321</sup> Shareholders have the right to seek an audit and take the board members personally to court, even if the corporation tolerates or is unable to take action against them.<sup>322</sup> However, there are a lot of improvements between the new and old versions of Ethiopia's commercial code. However, there is still room for improvement in comparison to the current South African, United Kingdom and Germany company legislation that covers the duties and liabilities of the board of directors. The lessons from company law in South Africa, the United Kingdom, and Germany will be covered in the next part, along with the gaps in the duties and liabilities of directors under the new commercial code.

#### **4.2.2. Directors' Duties under the new Ethiopian commercial law and Lessons from South African Company Law**

Articles 316 through 318 of the new commercial code outline the main duties of the board of directors, which are categorized into three groups: the duty of care and diligence, the duty of independent judgment, and the duty of loyalty. The new Ethiopian corporate legislation's Articles 318 through 322 also give additional director duties.

##### **A. The Director's duty of loyalty**

The following is the definition of the directors' duty of loyalty in the new Ethiopian commercial code: Directors must act in the best interests of all company shareholders and in a way that they

---

<sup>316</sup> Ibid

<sup>317</sup> Art. 331(1) of Commercial Code of Ethiopia, Proclamation No. 1243/2021

<sup>318</sup> Belete (n 140)

<sup>319</sup> Ibid

<sup>320</sup> Art. 325(1 and 2) of Commercial Code of Ethiopia, Proclamation No. 1243/2021

<sup>321</sup> Belete (n 140)

<sup>322</sup> Art. 329(1 and 2) of Commercial Code of Ethiopia, Proclamation No. 1243/2021

genuinely believe will most likely contribute to the company's development, according to Article 316 (1) of the FDRE Commercial Code. Additionally, boards must consider the company's long-term interests, those of its employees, those of its creditors, and the consequences on the environment and community, according to subsection two of the same article. In accordance with the South African Company Act's section 76(3)(b), this evidence clearly illustrated directors' obligations to act in the best interests of the company. The article also described the principle under South African case law, which includes the need to behave in the best interests of the firm and states that "company" refers to the company's shareholders.<sup>323</sup> This also states that directors must act in the existing shareholders' best interests while also considering their future interests. Future shareholders are brought up to highlight the importance of directors considering both short-term and long-term concerns. In addition to this the United Kingdom Companies Act Section 172 under the Duty to promote the success of the company, highlights the significance of taking into account the interests of various stakeholders, including customers, suppliers, employees, and the community. It urges directors to operate in the greatest long-term interests of the company as a whole and fosters a more responsible and balanced approach to corporate decision-making. The duties of loyalty are established by Ethiopian Commercial Code Article 316, which does not refer to it as the duty to act in the best interests of the company. This is because the duty of loyalty consists of several concepts with three essential components: They must refrain from using company advantages for their own gain, avoid getting personally involved in the company's business relationships with third parties, and protect the privacy of corporate information.<sup>324</sup>

Two additional common law obligations are contained in South African company law Section 76(3)(a) and are the duty to act in good faith and the obligation to act with purpose. A director's main obligations are to exercise good judgment, carry out their duties with honesty and behave in the company's best interests. This one qualifies the director for any additional duties and authorities.<sup>325</sup> Furthermore, despite the fact that the duty of good faith was included in the duty of loyalty of directors under article 316 (1) of the Ethiopian Commercial Code without any explanation, the failure to include the title of the duty of good faith along with a better

---

<sup>323</sup> Seedat (210) 37

<sup>324</sup> Schwartz, Mark S., Thomas W. Dunfee, and Michael J. Kline. 'Tone at the top: An ethics code for directors?' (2005) *Journal of Business Ethics* 58.1 79-100.< <https://rb.gy/rhxwoj>> accessed in 18 September 2022

<sup>325</sup> Ibid

explanation of the duty demonstrates that the concept was not given enough emphasis, despite the fact that it is critical for the entire duty of the board of directors as discussed in chapter three of the thesis. As a result, the article may borrow a phrase from South African and UK company law, such as "duty to act in the best interests of the company." Furthermore, the responsibility of good faith of directors should be better defined in Ethiopian company law to compel directors to behave in good faith.

### **B. The duty to exercise independent judgment**

The Article 317 provision of the FDRE Commercial Code lists numerous tasks and emphasizes the seriousness of the board of directors' duties.<sup>326</sup> Unless there are particular limitations established in the memorandum of association or by an agreement with the corporation, members of the board of directors must use independent and impartial judgment when performing their duties.<sup>327</sup> It is often stated in South African company law article 76 that directors have an independent judicial role; nevertheless, this notion was not specifically included in the South African company act, thus it is a good job that the new commercial code has included it. Section 172 of the United Kingdom company act also highlights the need for directors to exercise independent judgment. This means that directors should not be excessively influenced by the interests of a single shareholder or stakeholder group. Instead, they should make objective decisions that benefit the organization as a whole<sup>328</sup>. How much emphasis has been placed on the idea that directors' judgment should be independent while they carry out the different duties assigned to them by the company act is evident from the inclusion of independent judgment as a duty with its own title. The German Stock Corporation Act (Aktengesetz) as well addresses the role of directors to exercise independent judgment. Section 93 (1) of the act expressly states that the management board of the firm should handle its activities independently, with the company's interests serving as the primary guiding principle. It emphasizes the value of individual decision-making.<sup>329</sup>

---

<sup>326</sup> Article 317 (1 and 2) of The FDRE Commercial Code

<sup>327</sup> Ibid

<sup>328</sup> Section 172 of UK company act

<sup>329</sup> Section 93(1) of German stock corporation act

### C. The duty of care and diligence

Article 318 of Ethiopia's Commercial Code requires Board members to conduct themselves effectively and diligently. Members of the board of directors must diligently discharge their obligations.<sup>330</sup> The level of care and competence that a company director must show, as well as the level of diligence that might be reasonably expected of a person carrying out the duties of a company director, are used to measure the director's duty.<sup>331</sup> The article defines the standard as the entirety of knowledge, skills, and wisdom that a responsible board member should possess. This standard or measurement is subjective. However, this concept is also addressed by South African business law. As a result, a director must perform their responsibility with the degree of skill, care, and diligence that may be reasonably expected of someone with the considerable knowledge, skills, and experience that the director possesses, according to Section 76(3)(c) of the 2008 Act. It is challenging to develop a clear, objective criterion of the obligation because the duty of directors is highly subjective. Since South African duty and liability are only partially codified under South African business law, they can be interpreted through a number of court cases and used as precedent to consistently interpret and understand the notion. As a result, it is advisable to understand the concept under the commercial code by considering all scenarios and looking South African legal precedent that may be relevant to the directors' obligation to exercise reasonable care, skill, and diligence.

However In the United Kingdom, the Companies Act 2006's section 174 duty of care and diligence is widely regarded as an objective standard. It is required of directors to perform with the care, skill, and diligence that a reasonably careful individual in their position would perform. Directors are held to a standard of care that extends beyond their own personal expertise or experience. Instead, it considers both of them: The level of general knowledge, skill, and experience that could be expected by someone performing a director's duties for the company and the director's genuine broad knowledge, skill, and experience. So it is advisable to look the experience of United Kingdom that requires directors to exercise a level of care, skill, and diligence.in addition to this Section 93(1) of the German Stock Corporation Act's (Aktiengesetz) sets duty of care, skill, and diligence is widely regarded as an objective standard. In comparable circumstances, directors are required to act with the same care and diligence that a prudent and

---

<sup>330</sup> Ibid Article 318 (1and 2)

<sup>331</sup> Ibid

diligent businessperson would. It implies that directors are assessed according to what a prudent individual in their position would have done when faced with an identical situation. so It is important to remember that certain situations and elements might be taken into account when assessing a director's conduct. For instance, the scale and complexity of the business, understanding of the industry, and the experience of each director may all be important considerations for deciding on the right level of care.

However, it's better to have a dual subjective and objective standard Because a dual objective/subjective test uses fictitious knowledge and experience that would be reasonably expected of a person with the same function as the director, the acts of directors must be evaluated both objectively and subjectively in relation to their unique personal qualities. This involves taking into account each director's unique function within the particular organization and requiring all directors to adhere to a general standard of care.<sup>332</sup> A second advantage of a dual objective/subjective standard based on each director's particular role within the particular company is that it provides the courts with the appropriate discretion to take the director's function into account when making decisions. It enables the courts to make job-related distinctions amongst directors.<sup>333</sup> A dual standard can offer people who are aware of their incompetence a strong disincentive. They may no longer seek for office.<sup>334</sup>

#### **D. The Duty to avoid and Disclose conflict of interest**

The other responsibilities that prohibits directors from utilizing the company's assets, information, or business prospects for their own or others' benefit is the duty to avoid conflicts of interest. The new Commercial Code has two groups of provisions: prohibited and regulated transactions, which are meant to prevent conflicts of interest between the firm and its directors. Directors are prohibited, on the one hand, from making loans to corporations and from owning joint and several liability partnerships in businesses that are competitors,<sup>335</sup> or engage in either direct or indirect rivalry with the firm; however, a director may conduct business with a

---

<sup>332</sup> Zwinge, Tamo, Have Directors' Duties of Care and Skill Become More Stringent? What has Driven this Development? Is this Development Beneficial? An Analysis of the Duty of Care in the UK in Comparison to the German Duty of Care (October 20, 2009). Available at SSRN: <https://ssrn.com/abstract=1591590> or <http://dx.doi.org/10.2139/ssrn.1591590>

<sup>333</sup> Ibid

<sup>334</sup> Ibid

<sup>335</sup> Article 319-320 of The FDRE Commercial Code

corporation with the prior approval of the General Assembly.<sup>336</sup> In addition, each director must inform the board of directors of any circumstance that could result in a conflict between his and the company's interests, according to article 321 of the new commercial code.<sup>337</sup> South African Company Law, like the new Ethiopian Commercial Law, contains Sections 75 and 76(2)(a), which advise Directors to avoid dealings with the corporation's management, directors, or significant shareholders that could lead to conflicts of interest, and to avoid prioritizing their own interests over those of the corporation and its shareholders.<sup>338</sup> Moreover, as soon as practicable, such differences should be made public.

Directors are not allowed to share with anybody else any information they may have encountered while serving in that capacity without the company's permission.<sup>339</sup> As a result, Section 75 applies to all directors, including those who serve on board committees and audit committees as established under the 2008 Act.<sup>340</sup> If a director has a personal financial interest in the outcome of a topic to be discussed at a board meeting, or knows someone who does, they must declare that interest and any relevant facts under Section 75(5).<sup>341</sup> Contrary to article 321 of the Ethiopian Commercial Code, which did not outline the consequences of failing to disclose a conflict of interest, South African company law specifies that any agreement or resolution adopted by the board without such disclosure is null and void and is not enforceable unless it is approved by an ordinary resolution under section 75(7) or a court order under section 75(8).<sup>342</sup> As therefore, Ethiopian company law could learn from South African company law on the consequences that should be implemented when directors fail to disclose a conflict of interest when it arises.

In UK company act 2006 Duty to disclose an interest in a proposed transaction or arrangement: Under Section 177, a director who has a direct or indirect interest in a transaction or arrangement that the firm is considering must disclose that interest to the board.<sup>343</sup> Before the company completes the transaction, the director must make a declaration outlining the type and scope of their interest. If the director is unaware of the company's transaction or arrangement, or if he is

---

<sup>336</sup> Ibid

<sup>337</sup> Article 321 of The FDRE Commercial Code

<sup>338</sup> Section 75 and Section 76(2)(a), of the Companies Act 71 of 2008

<sup>339</sup> Ibid

<sup>340</sup> Ibid

<sup>341</sup> Section 75(5) of the Companies Act 71 of 2008

<sup>342</sup> Ibid section 75 (7) and 75(8)

<sup>343</sup> Section 177 of the UK company act 2006

unaware of his interest, no declaration is necessary. Additionally, if the other directors are already aware of the interest or if it is not reasonably anticipated to result in a conflict, no declaration is required.<sup>344</sup> If there was no declaration by the director under section 177, failure to make a declaration under this section constitutes a criminal offense.<sup>345</sup> Therefore Ethiopian company law could learn from United Kingdom company law as well. In German Concerning Avoiding Conflicts of Interest Even with the precise wording, it is evident that the provision under the German and South African laws does not in any way shield influenced or dependent acting. The South African code expressly regulates the duty to prevent self-dealing and conflicts of interest, whereas the German codification controls this principle under the requirement of the company's best interests.<sup>346</sup>

### **4.3 Directors' liabilities under the new Ethiopian commercial law and Lessons from South African, United Kingdom and German Company Law**

Directors, whether they are corporate members, are liable for unlawful activity while performing their official duties and may be held accountable in both civil and criminal courts. Regarding the board's civil liabilities, directors are the company's trustees and agents, and as such, they are accountable to the company under laws, meeting decisions, or both. Directors will be held jointly and severally liable with the Company for any violation of or failure to meet such obligations, as well as with the Company, any third-party creditors, and the Company's shareholders. Articles 325–330 of the new commercial code define the board of directors' main liabilities. The next sections will compare the director liabilities under the new commercial code to those under South African, UK, and German company law and look at whether there are any lessons to be learnt from the selected country's company law on the same themes being discussed.

#### **A. Liability towards the Company**

Article 325 of the new commercial law explicitly says that directors are jointly and severally liable to the firm for any injury caused by their misconduct while performing their duties.<sup>347</sup> As a result, the firm may file one or more of them and seek reimbursement for all damages. The law

---

<sup>344</sup> Ibid

<sup>345</sup> Section 182 of the UK company act

<sup>346</sup> Dr Stefan Eisele (2017) Codification of the Business Judgment Rule in Section 76 (4) Companies Act 2008: Comparing the South African with the German Approach *Published by the University of Cape Town (UCT)* <<https://open.uct.ac.za/server/api/core/bitstreams/1487505a-506c-4679-ba29-71609580cc9d/content>> accessed in 10 may 2024

<sup>347</sup> Article 325(1) of The FDRE Commercial Code

provides no objective criterion of culpability in this regard.<sup>348</sup> However, sub-article 2 of Article 325 requires the directors to establish that they behaved with due care and diligence. As a result, they could only avoid culpability by demonstrating that their actions were carried out with due care and diligence.<sup>349</sup> This possible explanation for directors is elaborated in Article 327 of the same regulations. Directors may not be held accountable if they made an informed business decision in good faith and quickly informed the external auditor of their disagreement. In the same way, section 77(6) of South African company law introduced the same concept by stating that a director's culpability is joint and several with that of any other person for the same act.<sup>350</sup> Furthermore, South African Company Law Section 77(9), on the other hand, empowers the court to release a director from liability for behavior that is neither willful misconduct or an intentional breach of trust, if the director acted honestly and reasonably or ought to have been considerably relieved from liability.<sup>351</sup> The statute of limitations for proceedings seeking to recover any loss, damages, or expenses for which a person is or may be held liable under Section 77(7) is three years. The Ethiopian Commercial Code did not expressly indicate the directors' responsibility statute of limitations, so the Civil Code was used to cover the gap. It would therefore be preferable for the commercial to investigate the scope of directors' liabilities and set a statute of limitations, taking lessons from South African company law.

### **B. Liability to shareholders and creditors**

Members of the board of directors may be held accountable by the company's shareholders for losses caused to one or more shareholders. Article 333 of the Ethiopian Commercial Code gives shareholders the right to sue board of directors.<sup>352</sup> In this case, the law is silent on whether shareholders can make a claim based on the directors' joint and several liability. Furthermore, if the company's assets are insufficient to pay creditors, directors are liable to creditors for any asset loss they create.<sup>353</sup> Even if these directors' liabilities are also stipulated in South African company law, Section 218(2) of the Companies Act states that "any person" who violated "any provision" of the Act is liable for compensating "any other person" for any loss or harm incurred.

---

<sup>348</sup> Belete (n 140)

<sup>349</sup> Ibid Article 325(2)

<sup>350</sup> Section 77(6) of the Companies Act 71 of 2008

<sup>351</sup> Section 77(9) of the Companies Act 71 of 2008

<sup>352</sup> Ibid Article 333

<sup>353</sup> Article 329 of The FDRE Commercial Code

The Companies Act, No. 71 of 2008 (the Act) protects members of a company's board of directors from personal liability for any loss or damage suffered by the company or its shareholders as a result of anything done or omitted to be done by the director in good faith and during the course of the director's performance of his duties. A lesson from South African company law might be applied by the new business code, holding directors liable for any wrongdoing.

In German. According to AktG 147, the shareholder meeting may vote to advise the company to claim damages against a director. Shareholders can vote to designate a special representative. Enforce a claim. The court may appoint a representative upon a minority's request.<sup>354</sup> In the United Kingdom, directors and management have a duty to the company. As a result, the company is the competent plaintiff to initiate an action claiming a breach of duty. "Derivative actions" are when the court uses its general "equity" powers to do justice. In certain cases, a shareholder may be able to take action on behalf of the company for its benefit.<sup>355</sup>

### **C. Criminal Liability of the Board of Directors**

According to Article 702(1) of the Ethiopian Criminal Code, anyone who is legally or contractually obligated to watch over or manage the property rights of others and purposefully causes harm to those property interests by abusing their authority or failing to perform their duties is punishable by a fine or immediate imprisonment.<sup>356</sup> If the crime was committed negligently, the perpetrator would pay a fine or spend six months of simple imprisonment.<sup>357</sup> If the criminal meant to financially profit himself or another party when committing the offense, they might face a minimum of one year in rigorous imprisonment and a maximum fine of 30,000 Birr.<sup>358</sup> The punishment should therefore be more severe depending on the circumstances. However, the Ethiopian company legislation does not specify the possibility of a criminal charge for breaching any obligation assumed over the board of directors. Any directors who continue to operate despite knowing that the organization is unable to pay its debts are breaking the law and may face criminal charges under South African company law. This is something that Ethiopian

---

<sup>354</sup> Bernard Black Brian Cheffins Martin Gelter Hwa-Jin Kim Richard Nolan Mathias Siems LEGAL LIABILITY OF DIRECTORS AND COMPANY OFFICIALS PART 2: *COLUMBIA BUSINESS LAW REVIEW* Vol. 2008 <<file:///C:/Users/hp/Downloads/SSRN-id1010307.pdf>> accessed 18 may 2024

<sup>355</sup> Ibid

<sup>356</sup> Article 702 of The Criminal Code of the Federal Democratic Republic of Ethiopia 2004

<sup>357</sup> Ibid

<sup>358</sup> Ibid

business laws may adopt from South African company law, along with other potential criminal liability issues.

In German law Section 993 of the German Companies Act 2006 establishes criminal sanctions on people who participate in fraudulent business activity. If a director violates their obligations and causes a financial loss to the firm, they may face breach of trust charges under 266 of the Criminal Code.<sup>359</sup> In addition to this Failure to file for insolvency in a timely manner is a criminal offense. Directors may face imprisonment for up to three years (or one year in the case of carelessness) or a fine. Furthermore, directors who are convicted of failing to file for insolvency will be barred from holding any future director posts for a period of five years. And regarding the civil liability If the firm suffers loss as a result of the directors' breach of duty, the insolvency administrator may hold them personally liable. Directors have severe liability for transactions at an undervalue or transactions detrimental to creditors, unless the bankruptcy administrator can effectively claw back the appropriate funds from the receiver under applicable claw back laws.<sup>360</sup> Payments made after the company became insolvent, which were not made with the diligence of a prudent businessperson even in an insolvency

- Failure to pay certain taxes and social security contributions
- Giving payments to shareholders that result in the company becoming unable to pay its debts when due
- Paying back statutory share capital to shareholders in violation of statutory capital maintenance rules, so Ethiopian company law learn something from this

#### **4.4 Conclusions**

Based on the study's findings, the researcher arrived at the following key conclusions regarding the duties and liabilities of the board of directors under Ethiopian corporate law. First, the basic tasks of the board of directors are specified in articles 316 through 318 of the new

---

<sup>359</sup> MANUEL LADIGES (2013) CRIMINAL LIABILITY OF DIRECTORS *Springerlink.com*  
[https://eu.docworkspace.com/d/sIDuPmKP\\_AaOMjblG](https://eu.docworkspace.com/d/sIDuPmKP_AaOMjblG) accessed 17 may 2024

<sup>360</sup> Andreas Lehmann (2023) Directors' Duties – Germany  
Considerations for Directors When a Company Is in Financial Difficulty *quirepattonboggs.com*  
[https://eu.docworkspace.com/d/sINaPmKP\\_Ac-TjblG](https://eu.docworkspace.com/d/sINaPmKP_Ac-TjblG) accessed 17 may 2024

commercial laws. As a result, despite being included in article 316 of Ethiopia's revised company law, the director's duty of loyalty did not include all three of its components: refraining from using corporate opportunities for personal gain, refraining from having a personal stake in business transactions the company enters with third parties, and maintaining the confidentiality of corporate information. As a result, because the entire concept refers to acting in the best interests of the company, as the article may be titled "Duty to Act in the Best Interest of the Company" and use a phrase from the chosen country's company law.

Furthermore, even though the duty of good faith was included in the duty of loyalty of directors under article 316 (1) of the Ethiopian Commercial Code without explanation, the lack of a title for the duty and a better explanation of the duty indicates that the idea was not given sufficient emphasis. The responsibility of directors to behave in good faith should be more explicitly defined in Ethiopian company law, as it is in the selected countries' company law.

Furthermore, Article 318 of Ethiopia's Commercial Code requires board members to behave diligently and with care. The article defines the standard as the entirety of knowledge, ability, and insight that a responsible board member should possess. This standard or measurement is subjective and open to interpretation. Therefore, it is preferable to comprehend the idea under the commercial code by taking into account every scenario by looking into the selected countries' legal jurisprudence that could be related to the directors' duty to exercise reasonable care, skill, and diligence to have dual subjective and objective elements while identifying the duty.

Furthermore, the two obligations of directors were included in the new commercial code articles 318 through 321 regarding the duty to avoid and disclose conflicts of interest. In contrast to Article 321 of the Ethiopian Commercial Code, which did not explain the consequences of failing to report a conflict of interest, under the South Africa company law, both duties are stipulated. However, the law also provides that any agreement or resolution adopted by the board without such disclosure is null and void and is not enforceable unless it is approved by an ordinary resolution under section 75(7) or a court order under section 75 of the South African company law. Thus, in order to understand the sanctions that ought to be applied when directors fail to report a conflict of interest when it arises, Ethiopian company law should learn from South African company law.

In UK Company act 2006 Duty to disclose an interest in a proposed transaction or arrangement: Under Section 177, a director who has a direct or indirect interest in a transaction or arrangement that the firm is considering must disclose that interest to the board. Before the company completes the transaction, the director must make a declaration outlining the type and scope of their interest. If there was no declaration by the director under section 177, failure to make a declaration under this section constitutes a criminal offense.

Second, in terms of director liabilities, the new Commercial Code's Articles 325 through 330 establish the board's core liabilities. Directors are so clearly accountable to the corporation jointly and severally under the terms of Article 325 governing liability towards the firm. Similar provisions for directors' liability are contained in selected countries' company laws, which require joint and several liability. The Ethiopian Revised Commercial Code does not include the option of being released from liability by demonstrating no deliberate misconduct or an intentional breach of trust if the director acted honestly, in contrast to other countries' company law. This further indicated that no deliberate misconduct or an intentional breach of trust if the director acted honestly and fairly or ought to have been considerably released from liability. Therefore, Ethiopia could learn from those countries' company legislation. Furthermore, the Ethiopian Commercial Code does not indicate when the directors are no longer liable due to the passage of time, as opposed to South African company law, which provides a three-year statute of limitations for claims. As a result, Ethiopian corporate law could also learn something from this.

Furthermore, members of the board of directors may be held liable by the company's shareholders for losses made to one or more shareholders, in addition to liability to creditors and shareholders. It is still unclear from the legislation whether shareholders may make a claim based on the directors' joint and several culpabilities, despite the fact that Article 333 of the Ethiopian Commercial Code allows the ability to sue the directors. It would be ideal if the legislation specified how shareholders might file a claim for damages. Directors are liable for the balance of a company's debt if its assets fall short of covering it, according to Commercial Code Article 329. Although South African company law already stipulates this, it also provides that directors are exempt from personal liability for any loss or harm incurred by the company or its shareholders as a result of anything they did or did not do in good faith while carrying out their

duties. The new Ethiopian business code may therefore be able to learn something from South African corporate law.

Furthermore, while Article 702(1) of the Ethiopian Criminal Code expressly indicated that the board of directors might be held criminally liable, the new Commercial Code did not adequately describe the possibilities of criminal liability and penalties based on the gravity of the breach. Therefore, it is preferable that business law adequately addresses and covers this gap. Furthermore, whereas Ethiopian law makes no mention of this, the selected countries' company law specifically allows criminal liability while directors continue to administer the corporation despite knowing it cannot pay its debts. As a result, exactly as those nations' company laws, the Ethiopian commercial code should hold directors legally liable for forcing the company to go out of business if it is unable to repay its debts. In German. According to AktG 147, the shareholder meeting may vote to advise the company to claim damages against a director. Shareholders can vote to designate a special representative. In the United Kingdom, directors and management have a duty to the company. As a result, the company is the competent plaintiff to initiate an action claiming a breach of duty. "Derivative actions" are when the court uses its general "equity" powers to do justice. In certain cases, a shareholder may be able to take action on behalf of the company for its benefit. Therefore, Ethiopian company law has to take something from the selected countries' company law.

#### **4.5 Recommendations**

The following recommendations are offered as a first step toward raising corporate governance standards and fixing the Revised Commercial Code's shortcomings in addressing contemporary issues with director duties and liabilities: -

- ❖ Directors must operate in the best interests of shareholders, which demands fiduciary behavior and informed decision-making. A duty to act in the best interests of the company and shareholders should be expressly mentioned in the title of provisions and thoroughly elaborated in Ethiopian commercial regulations, exactly as in the chosen nations' company law.

- ❖ Cognizant of the fact that Under Article 316 (1) of the Ethiopian Commercial Code, the duty of good faith was implicitly incorporated into the directors' duty of loyalty. The duty of directors to act in good faith should be more clearly defined in Ethiopian company law to enforce it, similar to South African company law.
- ❖ Recognize that the Commercial Code of Ethiopia's Article 318, which requires careful and diligent behavior from board members, is a subjective norm or measurement that is susceptible to interpretation. The business code of Ethiopia should provide objective criteria for the obligation by considering every circumstance covered by those selected countries' legal precedent regarding the obligation for directors to exhibit reasonable care, skill, and diligence. or dual subjective/objective standard that uses fictitious knowledge and experience that would be reasonably expected of a person with the same function as the director, the acts of directors must be evaluated both objectively and subjectively about their unique personal qualities. This involves taking into account each director's unique function within the particular organization and requiring all directors to adhere to a general standard of care. and based on each director's particular role within the particular company is that it provides the courts with the appropriate discretion to take the director's function into account when making decisions and it offers people who are aware of their incompetence a strong disincentive. They may no longer seek for office
- ❖ Being aware that, in contrast to the company legislation of those nations, which declares that any resolution or agreement issued by the board that does not include such information is unlawful and cannot be enforced until authorized, article 321 of the Ethiopian Commercial Code did not specify the consequences of failing to disclose a conflict of interest. Therefore, Ethiopian company law should create legislation to this effect to clarify the sanction that should be used when directors fail to disclose a conflict of interest when it develops.
- ❖ Cognizant of the fact, in contrast to those country's company law, directors are liable to the corporation jointly and severally under article 325's provision towards the company and failed to mention the option of being released from liability by demonstrating not deliberate misconduct or an intentional breach of trust if the director acted honestly. Ethiopia ought to take note of this and pass legislation that absolves the directors subject to a certain predetermined.

- ❖ Knowing that the board of directors' members may also be held liable by the company's shareholders for losses they caused to one or more shareholders and that the law does not yet clearly state whether shareholders may file a claim based on the directors' joint and several liability, the Ethiopian Commercial Code should expressly state how the directors' liabilities will be for the shareholders' claim.
- ❖ Recognize that while the board of directors is criminally liable under article 702(1) of the Ethiopian Criminal Code, the new Commercial Code did not completely define this potential or the associated punishment based on the gravity of the infraction. To render directors criminally liable, the Ethiopian Commercial Code should enact such laws.

## **Bibliography**

### **Books**

- Abera J, *Legal History of Ethiopia*, (Shama Books 2012 Addis Ababa).
- Abigail Levrau, *Corporate governance and the board of directors: a qualitative-oriented inquiry into the determinants of board effectiveness*, (Diss. Ghent University, 2007.) 41  
< <https://www.pdfdrive.com/corporate-governance-and-the-board-of-directors-e53316310.html>> accessed on 10 February 2024.
- Addis Ababa Chamber of Commerce, *Position of the Business Community on the Revision of the Commercial Code of Ethiopia* (Addis Chamber, 2008).
- Aglietta M, and Antoine R, *Corporate governance adrift: a critique of shareholder value*. (Edward Elgar Publishing, 2005). <<https://rb.gy/gp4hwhf>> accessed on 3 August 2022
- Bernard Black Brian Cheffins Martin Gelter Hwa-Jin Kim Richard Nolan Mathias Siems LEGAL LIABILITY OF DIRECTORS AND COMPANY OFFICIALS PART 2: COLUMBIA BUSINESS LAW REVIEW Vol. 2008<<file:///C:/Users/hp/Downloads/SSRN-id1010307.pdf>> accessed 18 May 2024.
- Bob Tricker and Robert Ian Tricker, *Corporate governance: Principles, policies, and practices*, (Oxford University Press, 2015.)
- Bob Tricker, *THE EVOLUTION OF CORPORATE GOVERNANCE* (Cambridge University Press,2020)
- Calder A, *Corporate governance: A practical guide to the legal frameworks and international codes of practice*. (Kogan Page Publishers, 2008) <<https://rb.gy/u4pjrj>> accessed on 5 August 2022
- Calder A. *Corporate governance: A practical guide to the legal frameworks and international codes of practice*, (Kogan Page Publishers, 2008.) <<https://rb.gy/s0uvsrI>> accessed on 6 July 2022
- Cassim FHI, Cassim M.F., Cassim R, Jooste R, Shev J, and Yeats J, *Contemporary Company Law*, 2<sup>nd</sup> ed (Juta and Company, Claremont 2012).
- Davis D, and Geach W, *Companies and Other Business Structures in South Africa*, (3<sup>rd</sup> ed, Oxford University Press Southern Africa (Pty) Ltd 2013 )
- Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L, and Burdette D, *Companies and other Business Structures in South Africa*, 3<sup>rd</sup>edn, (Oxford University Press of South Africa (Pvt) Ltd 2013)
- Deloitte, Z.A., *Duties of Directors* (Deloitte Touche Tohmatsu Limited, April 2013).

- Griffin S, *Company Law: Fundamental Principles* 3rd ed (London, Pearson Education Limited, 1991).
- GENERAL NOTICE, 'South African Company Law for the 21st Century Guidelines for Corporate Law Reform'(2004) STAATSKOERANT, NOTICE 11 83 OF 2004 < [https://www.gov.za/sites/default/files/gcis\\_document/201409/26493gen1183a.pdf](https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf) accessed on 15 April 2024
- Gulshan S.S. and Kapoor G.K, *Business law including Company Law*, 10th edn(New Age International Publishers New Delhi 2003).
- Harry C. Henn, *Laws of Corporation* (New York, West Group 1983) 3rd ed
- M, *Boards, governance and value creation: The human side of corporate governance*. (Cambridge University Press, 2007) <<https://rb.gy/tkvfbh> > 5 August 2022
- IBP *South Africa Company Laws and Regulations Handbook*, Vol. I. International Business Publishers, USA 2019).
- Jain DP, *Company Law*, 3rd edn (Konark Publishers Pvt Ltd 2004)
- Levrau A, *Corporate governance and the board of directors: a qualitative-oriented inquiry into the determinants of board effectiveness*, (Diss. Ghent University, 2007.)< <https://www.pdfdrive.com/corporate-governance-and-the-board-of-directors-e53316310.html>> accessed in 6 July 2022
- Mäntysaari P, *Organising the firm: theories of commercial law, corporate governance and corporate law*, (Springer Science & Business Media, 2011.) < <https://rb.gy/omjqsq>> accessed in 6 July 2022
- Paul L.Davies, Sarah.W and Eva. W,*Gower and Davies, Principles of Modern Company Law* (Sweet and Maxwell Ltd 2008).
- Peter W, *Background Documents of Ethiopian Commercial Code of 1960*, (Faculty of Law, Haile Selassie I University 1974).
- Roberts J, *Agency theory, ethics and corporate governance. Corporate Governance: Does Any Size Fit?.* (Emerald Group Publishing Limited, 2005) <<https://rb.gy/3tzvbr>> accessed in 6 July 2022
- Stephen G, Sandra E. and Alstair H, *Charles Worth's Company law*, 18<sup>th</sup>edn, (Sweet and Maxwell Ltd2011).

- The Companies Act No. 71 of 2008, An Explanation Guide, Department of Trade and Industry (2010)

## Articles

- Addis Ababa Chamber of Commerce, Position of the Business Community on the Revision of the Commercial Code of Ethiopia (2008) 7.
- Andreas Lehmann (2023) Directors' Duties – Germany Considerations for Directors When a Company Is in Financial Difficulty [squirepattonboggs.com](http://squirepattonboggs.com)
- Ashenafi E, 'Financial Service Code to Fully Liberate Financial Sector' Ethiopian Reporter (Addis Ababa March 19 2022).
- Barry D Baysinger, and Butler N Henry, 'Corporate governance and the board of directors: Performance effects of changes in board composition' (2019) Corporate Governance. Gower,. 215-238  
<http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.962.1155&rep=rep1&type=pdf>  
> accessed in 7 November 2023 .
- Baysinger B, and N Henry B, 'Corporate governance and the board of directors: Performance effects of changes in board composition' (2019) Corporate Governance Gower  
<<http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.962.1155&rep=rep1&type=pdf>> accessed in 7 July 2022.
- Bekink M, An Historical Overview of the Director's Duty of Care and Skill: From the 19 Century to the Companies Bill of 2007, 20SA MercLJ, (2008)
- Belete M, THE NEW ETHIOPIAN COMMERCIAL CODE: UNCOVERING THE MAJOR CHANGES IN COMPOSITION, ROLE, AND ACCOUNTABILITY OF THE BOARD OF DIRECTORS( 2022) Commercial Law Blog <<https://www.abyssinialaw.com/blog-posts/itemlist/user/9359-misganawbelete>> accessed in 8 July 2022
- Bidie SS, Director's Duty to Act for a Proper Purpose in the Context of Distribution under the Companies Act 71 of 2008 PER/PELJ (2019).
- Bouman N, Board Committees, Without Prejudice (March 2010)
- Cassidy J, Models for reform: the director's duty of care in a modern commercial world, Stellenbosch Law Review Vol.20, (2009)
- Clarke T, 'Theories of corporate governance: The Philosophical Foundations of Corporate Governance' (2004) Oxon 12.4<<https://www.academia.edu/download/6742768/theoriesofcorporategovernancepreface.pdf>> accessed in 26 July 2022

- Coetzee L and Tonder J.L., Advantages and Disadvantages of Partial Codification of Directors' Duties in the South African Companies Act 71 of 2008, *Journal of Judicial Science*, (2016)
- Coetzee L, Directors fiduciary duties and the common law, *Obiter* vol.37 no.2 (June 2016).
- D. Kosnik R,' Greenmail: A study of board performance in corporate governance.' (1987) *Administrative science quarterly*.< <https://www.jstor.org/stable/pdf/2393124.pdf>> accessed in 8 July 2022
- Dbe A.' Regulating the Conduct of Directors', *Journal of Corporate Law Studies* (2010).
- Dekker Hofmeyr C, 'Corporate Governance: A Guide for Directors' (2021)CDH < <https://www.cliffedekkerhofmeyr.com/export/sites/cdh/en/sectors/downloads/Corporate-Governance-A-Directors-Guide.pdf>> accessed in 25 July 2022
- Donaldson L, and H. James D, 'Stewardship theory or agency theory: CEO governance and shareholder returns' (1991) *Australian Journal of management* 16.1< <https://www.academia.edu/download/33569543/rprnts.stewardshiporagency.pdf>> accessed in 26 July 2022
- Donaldson T, and Preston L,' The stakeholder theory of the corporation: Concepts, evidence, and implications' (1995) *Academy of management Review* < <https://sci-hub.hkvisa.net/10.5465/AMR.1995.9503271992>> accessed in 6 July 2022
- Donaldson,L, and James D, 'Stewardship theory or agency theory: CEO governance and shareholder returns' (1991) *Australian Journal of management* < <https://journals.sagepub.com/doi/abs/10.1177/031289629101600103>> accessed in 7 July 2022
- E.J, 'Directors' duties: negligence and the business judgment rule.' (2007) *SA Mercantile Law Journal* <https://rb.gy/jnyn7s>> 17 august 2022
- Endale A, 'A Bird's Eye View of the Revised Commercial Code' (2022) *Ethiopian Business Review* < <https://ethiopianbusinessreview.net/a-birds-eye-view-of-the-revised-commercial-code/>> accessed in 4 July 2022
- Fekadu P, Emerging Separation of Ownership and control in Ethiopian Share Companies: Legal and Policy Implications, *MizanLaw Review*, Vol. 4 No, (June 2010).
- Fekadu Petros, 'The New Ethiopian Commercial Code: A Highlight of Major Changes'(2022) Fekadu Petros & Partner Law Office< <https://fekaduandpartners.com/download/the-new-ethiopian-commercial-code-a-highlight-of-major-changes.pdf>.
- GENERANL NOTICE, 'South African Company Law for the 21<sup>st</sup> Century Guidelines for Corporate Law Reform' (2004) STAATSKOERANT, NOTICE 11 83 OF 2004< [https://www.gov.za/sites/default/files/gcis\\_document/201409/26493gen1183a.pdf](https://www.gov.za/sites/default/files/gcis_document/201409/26493gen1183a.pdf)> accessed in 25 July 2022

- Glinkowska B, and Kaczmarek B, 'Classical and modern concepts of corporate governance (Stewardship Theory and Agency Theory)' (2015): Management
- Harry C. Henn, Laws of Corporation (New York, West Group 1983) 3rd ed P. 612
- Havenga M, 'Directors' fiduciary duties under our future company-law regime.,(1997) S. Afr. Mercantile LJ 9< [https://heinonline.org/hol-cgi-bin/get\\_pdf.cgi?handle=hein.journals/safrmerlj9&section=36](https://heinonline.org/hol-cgi-bin/get_pdf.cgi?handle=hein.journals/safrmerlj9&section=36)> accessed in 25 July 2022
- Havenga, M 'The business Judgment Rule Should we follow the Australian example?' (2000) S A. Merc L.J.25.
- Havenga, M.' Director's Exploitation of Corporate Opportunities and the Companies Act 71 of 2008' Journal of South African Laws (2013).
- Heath J and Norman W, 'Stakeholder Theory, Corporate Governance and Public Management: What can the History of State-Run Enterprises Teach us in the Post-Enron era?',(2004) 53(3), <<https://rb.gy/dkiunm>> accessed in 6 July 2022
- Howard S. Company Directors Duties and Responsibilities, Journal of Business law, Vol. 13 part 3 (2005).
- Humera K, 'A literature review of corporate governance: In International Conference on E-business, management and Economics' (2011) vol. 25, no. 1, pp. < <https://rb.gy/oytnnh>> accessed 4 July 2022
- Hussien T, Overview of Corporate Governance in Ethiopia, The Role, Composition and Remuneration of Board of Directors in Share Companies, Mizan Law Review, Vol. 6 No. 1 (June 2012) .
- J Henning J, 'The South African close corporation under the Companies Act of 2008.' (2009) Amicus Curiae<[https://sas-space.sas.ac.uk/2911/1/Amicus80\\_Henning.pdf](https://sas-space.sas.ac.uk/2911/1/Amicus80_Henning.pdf)> accessed in 25 July 2022
- Johan D, Beware of Shadow Directors, without Prejudice, Vol. 17 No. 11 (2017).
- Joseph Heath and Wayne Norman, 'Stakeholder Theory, Corporate Governance and Public Management: What can the History of State-Run Enterprises Teach us in the Post-Enron era?',(2004) 53(3), <<https://rb.gy/dkiunm>> accessed in 6 July 2022
- Kathy K., The Regulation of Shadow Directors, 22 S.A. Mercantile Law Journal, (2010).
- King Committee on Corporate Governance, and Institute of Directors (South Africa) King Report on Corporate Governance for South Africa (King II Institute of Directors in Southern Africa, 2002.)
- Kleitman Y, 'Shareholders Actions', Without Prejudice vol.18 no.3 (April 2018).
- Letza S, 'Corporate governance theorising: limits, critics and alternatives' (2008) International Journal of law and management <<https://www.emerald.com/insight/content/doi/10.1108/03090550810852086/full/html>> accessed in 26 July 2022

- Locke N.' Shadow Directors: Lessons from Abroad', 14 S.A. Merc L.J. (2002).
- Loughrey, Joan. 'The director's duty of care and skill and the financial crisis. Directors' duties and shareholder litigation in the wake of the financial crisis' (2012) Edward Elgar Publishing
- Mark S, Dunfee T, and Kline M, 'Tone at the top: An ethics code for directors?' (2005) Journal of Business Ethics 58.1.< <https://rb.gy/rhxwoj>> accessed in 18 September 2022
- Minga N, Rethinking Corporate Governance in Ethiopia, University of Witwatersrand (2008) < <http://dx.doi.org/10.2139/ssrn.1264697>> accessed 4 July 2022
- Mohiudeen S, 'The effect of the partial codification of the common law duties of directors in the companies Act 71 of 2008 on the liability of directors' (2018) < <https://rb.gy/o5yoak>> accessed in 05 august 2022
- Muchlinski P. The Development of German Corporate Law Until 1990: An Historical Reappraisal. German Law Journal. 2013;14(2):339-379. doi:10.1017/S2071832200001838
- Muswaka L, 'Corporate governance under the South African Companies Act: a critique' (2012) Proceedings of World Business and Economics Research Conference. <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2184678](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2184678)> accessed in 25 July 2022
- Muswaka, L, Shielding Directors against Liability Imputations: The Business Judgment Rule and Good Corporate Governance,Speculum Juris(2013)
- Petros F, 'The New Ethiopian Commercial Code: A Highlight of Major Changes' (2022) Fekadu Petros & Partner Law Office< <https://fekaduandpartners.com/download/the-new-ethiopian-commercial-code-a-highlight-of-major-changes.pdf>> accessed in 5 July 2022
- Ramsay, I, Corporate Governance and Duties of Company directors, Center for Corporate Law and Securities Regulation, Faculty of Law, University of Melbourne (1997).
- Scott Leonard and David Webster (2009) Overview of Directors' Duties under the Companies Act 2006 accessed in 1 may 2024
- SeyoumY, On Formation of Share Companies in Ethiopia, Journal of Ethiopian Law, Vol. 20, Addis Ababa University, (July 2008) .
- Tsegaye B, 'A Brief History of the Ethiopian Legal Systems - Past and Present' (2013). International Journal of Legal Information, 2013, Duquesne University School of Law Research Paper No. 2017-07,< <https://ssrn.com/abstract=3088643>> accessed in 4 July 2022
- Valeria N, 'Corporate governance and board of directors: The effect of a board composition on firm sustainability performance' (2019)" Journal of Cleaner Production <<https://www.sciencedirect.com/science/article/pii/S0959652619325879>> accessed in 8 July 2022

- Zaman R, 'Fiduciary duty or loyalty? Evidence from co-opted boards and corporate misconduct.' (2021) Journal of Corporate Finance < <https://rb.gy/lrtwov>> accessed in 15 august 2022

## Dissertations

- ASHAGRIE B, 'CORPORATE GOVERNANCE IN BRANCHES OF FOREIGN COMPANIES IN ETHIOPIA: ANY DIFFERENT FROM LOCAL ETHIOPIAN COMPANIES?' (A Master's Thesis Submitted to School of Graduate Studies of Addis Ababa University in Partial Fulfillment of the Requirements of Masters of Law (LL.M),2014)
- Besirat Teklu 'Disqualification of Directors and Executive Officers as a Tool to ensure Good Corporate Governance in Ethiopia' (A Thesis Submitted to Addis Ababa University, College of Law and Governance, School of Law, in Partial Fulfillment of an LL.M degree in Business Law 2016)
- Bibi Kaudeer A, 'Does the role and duties of the business rescue practitioner as conferred by the South African Companies Act 71 of 2008 give rise to conflicts with respect to the powers and duties of directors during business rescue proceedings?' (MS thesis. University of Cape Town, 2016) < <https://rb.gy/hdzzoz>> accessed in 05 august 2022
- Hussein Ahmed Tura, 'Corporate Governance In Ethiopian Share Companies: What Should The Future Look Like?'( A Master's Thesis Submitted to School of Graduate Studies of Addis Ababa University in Partial Fulfillment of the Requirements of Masters of Law (LL.M),2011) 3
- Kefene G, 'Powers and Liabilities of Directors under the Commercial Code of Ethiopia' (LLM Thesis, Addis Ababa University, 2007).
- Kleynhans A, 'The Corporate Opportunity Rule, A corporative Study' (Thesis Submitted at University of South Africa,2016).
- Lucian Carciumaru M, 'An Assessment of the Impact of Corporate Governance Codes and Legislation on Directors and Officers Liability Insurance in South Africa' ( A dissertation submitted to the Faculty of Commerce, Law and Management of the University of the Witwatersrand, in fulfilment of the degree of Master of Commerce, 2009. < <https://rb.gy/2msvbq>> accessed in 17 august 2022
- Mekonnen S, 'Rights, Duties and Responsibilities of Directors in Financial Sectors of Ethiopia: With Special Emphasis on the Banking Sector' (LLM, Thesis, Addis Ababa University, 2009).
- Nigusie T, 'Major Problems Associated with Private Limited Companies in Ethiopia' (LLM Thesis, Addis Ababa University, 2009).
- Seedat F, 'Section 76 of the Companies Act 71 of 2008 as a mechanism of enforcement for the King IV Code on corporate governance for South Africa.' (This

dissertation is submitted in fulfilment of the requirements for the degree of Master of Laws, UNIVERSITY OF KWAZULU-NATAL 2019) < <https://rb.gy/ohcaug>> accessed in 15 august 2022

- Turner, John D. (2017) : The development of English company law before 1900, QUCEH Working Paper Series, No. 2017-01, Queen's University Centre for Economic History (QUCEH), Belfast
- Yeats J, 'The effective and proper exercise of appraisal rights under the South African Companies Act, 2008: developing a strategic approach through a study of comparable foreign law' (Thesis presented for the degree of DOCTOR OF PHILOSOPHY, Commercial Law Department at UNIVERSITY OF CAPE Town, 2016)  
<[https://open.uct.ac.za/bitstream/handle/11427/20301/thesis\\_law\\_2016\\_yeats\\_jacqueline.pdf?sequence=1](https://open.uct.ac.za/bitstream/handle/11427/20301/thesis_law_2016_yeats_jacqueline.pdf?sequence=1)> accessed in 25 July 2022

## Legislation

- Banking Business Proclamation, 2008, Proclamation No. 592, Federal Neg. Gaz. Year 14, No 57
- Companies Act 71 of 2008
- Ethiopian Banking Law Proclamation No. 592/2008.
- German Stock Corporation Act 2006
- The 1960 Ethiopian Civil Code
- The 1960 Ethiopian Commercial Code
- The Companies Act 2006 of U.K.
- The new Commercial Code of Ethiopia, Proclamation No. 1243/2021.

## Cases

- Drouzhba Ltd v. Wiseman and Anor [2006] EWHC 2708 (QB).
- Heath, P. In Re Smith Vs Fawcett Ltd Lord Green MR said: 2.' < <https://rb.gy/9cfpad>> accessed in 15 august 2022
- M Havenga' Directors exploitation of Corporate Opportunities and the Companies Act 71 of 2008' (2013) 2 TSAR at 257-268 citing Boardman v Phipps 1967 (2) AC 46, 1966 [3] A11 ER 721 (HL)
- Phillips vs Fieldstone Africa (Pty) Ltd and Another 2004 (3) SA 465 (SCA) 31< <https://rb.gy/02kyj5>> accessed in 15 august 2022

- Regal Hastings v Gulliver 1942 [1] A11 ER 378; Da Silva and Others v Ch Chemicals (Pty) Ltd 2008 (6) SA 620 (SCA).
- *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 <<https://rb.gy/gj0qdw>> accessed in 17 august 2022
- Visser Citrus (Pty) Ltd v Goede Hoop Citrus (Pty) Ltd and Others 2014 5 SA.
- Williams and Others v. Natural Life Health Foods Ltd. and Others, The Times, January 9, 1997.