





position of directors in a company was described in the English case of *Forest of Dean Coal Mining Company*<sup>92</sup> thus:

Directors have sometimes been called trustees, or commercial trustees, and sometimes they have been called managing partners. It does not matter what you call them so long as you understand what their true position is, which is that they are really commercial men managing a trading concern for the benefit of themselves and all the other shareholders in it.

Perhaps, a most interesting description of the status of directors in a company was given in the old English case of *Imperial Hydropathic Hotel Co., Blackpool v. Hampson*<sup>93</sup> thus:

...when persons who are directors of a company are from time to time spoken of by judges as agents, trustees, or managing partners of the company, it is essential to recollect that such expressions are used not as exhaustive of the powers or responsibilities of those persons, but only as indicating useful points of view from which they may for the moment and for the particular purpose be considered points of view which they seem for the moment to be either cutting the circle or falling within the category of the suggested kind. It is not meant that they belong to the category, but that it is useful for the purpose of the moment to observe that they fall pro tanto within the principles which govern that particular class.

The Nigerian case law have towed this line of reasoning in a number of cases. For example, in *Okeowo & Ors v. Miglore & Ors*<sup>94</sup>, it was held that they are trustees as they act as trustees to the company's properties and monies and they must act thereto with utmost good faith. Nigerian courts have also qualified directors as agents of the company in a number of cases like *Trenco (Nig) Ltd v. African Real Estate & Investment*,<sup>95</sup> in the case of *Alphonsus Oriebosi v. Andy Sam Investment Co. Ltd*<sup>96</sup> it was held that they can be referred to as agents because they act on behalf of the company and the company can be vicariously liable for their actions.<sup>97</sup> Yet, it seems that they are much more as they wear different hats within a company, the Supreme Court of Nigeria in *Yalaju Amaye v. A.R.E.C Ltd*<sup>98</sup> per *Nnaemeka Agu* held that the better view is that directors are agents, trustees and fiduciaries of the company.

Thus, it seems that the status and influence of company directors cannot be over emphasized as they wear different hats within the company and it is almost impossible for the company to act without the active participation and knowledge of the directors as they actively manage the affairs of the company, monitor and supervise the activities of the corporate employees and are the brain of the company dictating corporate strategy.<sup>99</sup>

In the course of the exercise of their duties, directors as decision makers exercise a lot of discretion in managing the affairs of the company. As humans that are fallible, innocent mistakes can occur even when exercising their fiduciary duty and acting in what they believe to be in the best interest of the company. The business judgment rule originally

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<sup>92</sup> (1878) 10 Ch.450 Per Jessel M.R

<sup>93</sup> (1882) 23 ChD 1at 12

<sup>94</sup> (1979) ALL NLR 282

<sup>95</sup> (1978) ALL NLR 124

<sup>96</sup> (2014) JELR 36415 CA, (2014) LCN 7310 CA

<sup>97</sup> *Alphonsus Oriebosi v. Andy Sam Investment Co. Ltd* (2014) LCN 7310 CA

<sup>98</sup> (1990)4NWLR (pt.145)422 SC

<sup>99</sup> Irrespective of the hat that directors wear in a company, what is not in doubt is that they are the brain of the company. Lord Denning in *H L Bolton & Co v. T J Graham & Sons* (1957) 1 QB 159 held that a company can be likened to a human body with brain and limbs. He said directors are the brains of the company which controls what it does and others within the company are like limbs which functions on the command of the brain. A cursory look at Nigerian case law shows that it aligns with this view. See *Adeniji v. State* (1992) 4 NWLR pt. 597, p.53, *Delta Steel Nigeria Ltd v. American Computer Tech Inc.* (1999) 4 NWLR pt. 597

developed in the United Kingdom and adopted across jurisdictions offers protection to directors when their actions and decisions affect the company negatively so long as there is no violation of the law or obvious act contrary to the company's interest. Nevertheless, it does not excuse wrongful behaviour on the part of directors. The rule was richly espoused in the US derivative case of *Re Walt Disney Co. Derivative Litigation* and provides that there is a rebuttable presumption in favour of company directors acting in good faith and in the best interest of the company at all time.

This article shall therefore discuss the role of directors especially as fiduciaries to the company which is foundational to the discretionary powers they enjoy. The article shall analyse the Walt Disney case where the business judgment rule was richly espoused in order to fully understand the application of the rule. The article also discusses the application of the rule in South Africa which as an African country shares a history with Nigeria as commonwealth countries. Finally, this article shall discuss the Nigerian company laws to determine whether the business judgement rule is applicable and to what extent. This is important because the business judgement rule is a pro corporate governance principle which can enhance the smooth running of corporations.

### Legal Materials and Methods

In analysing the business judgement rule and the fiduciary duty as espoused in the Walt Disney Derivative case and the Nigerian context, this article uses the juridical normative method, which analyses the Walt Disney case in the light of the business judgement rule and examines the application of the rule under the Nigerian company law.

Legal materials to be analysed are the Companies and Allied Matters Act 2020 of Nigeria, the Company's Act of South Africa. Also, case law from different jurisdictions like the US, UK, South Africa and Nigeria will be used. Also, relevant journal articles and text are also used.

### Results and Discussions:

#### Directors as Fiduciaries

While specific duties of directors are stated in the memorandum and articles of association, the general statutory duties are provided in the relevant statutes;<sup>100</sup> the basic duty of directors is the fiduciary duty upon which all other duties are based. This is because when the investor or business owner engages another person (director) to assist in the running of his business upon agreed terms, such a person (director) owes much more than a contract and must loyally serve the interest of the owner.<sup>101</sup> The fiduciary duty is expressed in terms of loyalty, integrity, good faith,<sup>102</sup> trust; confidence, acting in company's interest,<sup>103</sup> faithfulness, disclosure, knowledge and skilfulness.<sup>104</sup>

Another perspective to the fiduciary duty is that it is not expressed only through a positive act but also expressed by an omission to act if the circumstances suggest so. In *Regentcrest Ltd v. Cohen*,<sup>105</sup> the court in stating the subjectivity of directors' duty to act in the best interest of the company held that the pertinent question is whether directors believed their actions or omissions was in the best interest of the company. This goes to buttress the point that director's duty can be expressed through an omission.

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<sup>100</sup> There are general common law duties but most of which has been incorporated into statutes in countries like Nigeria.

<sup>101</sup> Patrick D. Okonmah, 'Directors as fiduciaries Under Nigerian Company Law' (1997) *Tilburg Law Review* 181

<sup>102</sup> Section 305 (1) Companies and Allied Matters Act 2020, *Okeowo v. Migliore* (1979) 11SC 133

<sup>103</sup> Section 305 (3) Companies and Allied Matters Act 2020

<sup>104</sup> See generally Section 305 Companies and Allied Matters Act 2020

<sup>105</sup> (2001) I.B.C.L 80 at 1056

The concept of fiduciary itself evolved from the equitable principles of trust where a party is vulnerable and allows another party to act for it based on trust.<sup>106</sup> It is expressed in terms of loyalty, integrity, good faith, trust; confidence, acting in company's interest, faithfulness, disclosure, knowledge and skilfulness. The fiduciary duty has been given validation by both the courts and various legislations on corporate law across different jurisdictions.

### Directors' Fiduciary Duty under the English Law

It is settled under the English law that directors have a duty of loyalty to the company and must avoid any form of conflict of interest. In the old English case of *Cooks v. Deeks*<sup>107</sup> the extent of conflict of interest was tested. Here, three directors took a railway line construction contract in their own names instead of the company's name to exclude a fourth director from the business and interestingly, use their votes as shareholders to ratify their action. It was the opinion of the Privy Council that their action was a fraud on the minority shareholder and conflict of interest precluded their ability to forgive themselves. A more recent English case on conflict of interest is the case of *JJ Harrison (Properties) Ltd v. Harrison*<sup>108</sup> where the conveyance by a company of some properties to one of its directors was set aside by the trial court and the director was held to account for the profits made on the sale of the property. In addition, it was shown that the director failed to make full disclosure to the company with respect to the value of the property. Although, the director appealed the decision on the grounds that the suit was statute barred based on the provisions of the Limitation Act 1980 and also on the ground that his defence of laches was rejected by the court; His appeal was dismissed and the court reiterated that when a director disposes a company property in breach of his fiduciary duty, such a director will be treated as a trustee of such property thus, the company is liable to recover the property or proceeds of the property held in trust but which was converted by the trustee.<sup>109</sup> The director's appeal was therefore dismissed.<sup>110</sup>

Similarly, in *Bhullar v. Bhullar*<sup>111</sup> a director established a company to buy a car park beside one of the company's properties, while the family company as a result of an existing family feud had resolved not to make any more investment in properties. Yet, it was held that the director ought to have disclosed to the company as the car park was an opportunity in line with the company's line of business. Thus, the director was held to have breached the conflict-of-interest duty and thus liable to make restitution to the company for the profits made.

It seems that directors can be liable for breach of duty even when they are no longer with the company so far as the act was done while still with the company. The case of *British Midland Tool Ltd v. Midland International Tooling Ltd*<sup>112</sup> suggests that directors preparing to enter into competition with the company after leaving the company are liable for breach of duty. In that case, some former directors of British Midland Tool Ltd were found liable of conspiracy and breach of duty when they planned to set up a rival company while engaged as directors and eventually did set up the company upon resignation. This position was reinforced in the case of *Shepherds Investment Ltd v. Walters*<sup>113</sup> where the claimant company brought an action against its erstwhile directors for breach of implied duty of fidelity and breach of fiduciary duty. The claimant company was an investment fund, and by 2003 began considering extending its business into whole-life policy market. Same 2003, three of its directors started discussions on establishing their own firm which would trade in whole-life policies and started preliminary

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<sup>106</sup> Babajide S. Shoroye 'Directors as Trustees of Company's Powers and Properties: Understanding the Justification for Fiduciary Duties'. (2022) 12 *Developing Country Studies*, No.5 ISSN 2225-0565

<sup>107</sup> (1916) 1AC 554

<sup>108</sup> (2002) 1BCLC 162

<sup>109</sup> It should be noted that the company also cross appealed and this was allowed in part.

<sup>110</sup> See also *Deg-Deutsche Investments v. Konshy* (2002) 1BCLC 478

<sup>111</sup> (2003) EWCA Civ 424

<sup>112</sup> (2003) 2 BCLC 523 at 560

<sup>113</sup> (2006) EWHC 836

steps towards actualising the plan after which two of the directors resigned. The new company was incorporated before the third director resigned. The court held that a director who intends to resign to set up a rival business must disclose as soon as the intention becomes irrevocable and thus held the directors liable.<sup>114</sup>

In *Re Barings PLC (No5)*<sup>115</sup>, it was held that director's duty extends to providing adequate supervision to the employees and also putting in place an effective risk management system. In this case, a futures trader secretly conducted unauthorized trades on behalf of the company (the Barings Bank). Three London directors had ignored a warning about the activities in Singapore which eventually led the company into bankruptcy. Subsequently, the directors were sought to be disqualified under the Company Directors Disqualification Act 1986 on the grounds of unfitness. It was held both by the high court and subsequently by the court of appeal that the directors' duty of care extends to acquainting themselves with the company's affairs and supervising appropriately, thus the directors in this instance were unfit to manage company's affairs.

### Directors' Fiduciary Duty in the United States

In the American case of *Hughes v. Northwestern University*,<sup>116</sup> the Supreme Court vacated the decision of the Court of Appeal and held that there was a breach of fiduciary duty under the Employment Retirement Income Security Act (ERISA). The plaintiffs had sued the defendant for breach of fiduciary duty for offering an expensive investment option when there were cheaper options. Both the trial court and the Court of Appeal had decided that there was no breach because the plaintiffs were not forced to invest in the expensive plan as they had the option to choose a cheaper investment plan. However, it was the opinion of the Supreme Court that a fiduciary's duty includes the duty to monitor and remove poor investments from the plan and failure to do so constitutes a breach of fiduciary duty under the ERISA. In *Smith v. Van Gorkem*<sup>117</sup> it was emphasized that the duty of directors entails making informed decisions with respect to the affairs of the company and it will be a breach of duty to act in ignorance,<sup>118</sup> though this case was on duty of care and skill. Knowledge is key and part of discharging their duty of care means that they must take steps to keep abreast of information that will benefit the company. It must be seen that they exercise due diligence and care in making decisions for the company. Personal interest must not clash with company's interest.

Similarly, the importance of the fiduciary role of a director was examined in the case of *Guth v. Loft*<sup>119</sup> where the company's director saw a business opportunity for the company but diverted same for himself instead. Guth was the president of Loft Inc. Loft Inc buys cola syrup from Coca Cola but Guth after Coca Cola failed to give a generous discount, decided to buy from Pepsi. However, before taking steps to buy from Pepsi, Pepsi went bankrupt and Guth bought over Pepsi in his personal capacity and subsequently with the aid of Loft Chemist formulated the Pepsi syrup recipe and sold it to Loft Inc. He was subsequently sued by Loft Inc.'s shareholders for breach of his duty of loyalty. His act of buying Pepsi for himself instead of Loft was deemed to be an act of disloyalty. The Delaware Supreme Court held that he breached his fiduciary duty by taking an opportunity the company was interested in. The court went further:

On the other hand, it is equally true that, if there is presented to a corporate officer or director a business opportunity which the corporation is financially able to undertake, which is, from its

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<sup>114</sup> *Framlington Group Plc v. Anderson* (1995) 1BCLC 475 note the earlier position in *Balston Ltd v. Headline Filters Ltd* (1990) FSR 385 which held that directors can take simple preparatory steps to establishing a rival business while acting as a director.

<sup>115</sup> (1999) 1BCLC 433

<sup>116</sup> 595 US 2022

<sup>117</sup> 488 A.2d 858 (1985)

<sup>118</sup> See also *Moran v. Household Intern Inc.* 490 A. 2d 1059 (1985)

<sup>119</sup> 5A.2d 503, 510 (Del.1939)

nature, in the line of the corporation's business and is of practical advantage to it, is one in which the corporation has an interest or a reasonable expectancy, and, by embracing the opportunity, the self-interest of the officer or director will be brought into conflict with that of his corporation, the law will not permit him to seize the opportunity for himself.

### Directors' Fiduciary Duty in South Africa

The South African company jurisprudence also affirms the existence and importance of director's fiduciary role in the company.<sup>120</sup> In fact, it gives a broad perspective to the fiduciary duty and is contextual with factors like power, vulnerability, discretion and influence being considered by the courts in arriving at a decision in specific cases.<sup>121</sup> For example, its scope was really explored in the case of *Volvo (Southern Africa) Pty Ltd v. Yssel*<sup>122</sup>. In this case, the respondent was employed by the plaintiff company as its IT manager but the employment was through H, a third party labour agent suggested by the plaintiff. The relationship between the company and the labour agent was regulated by a written agreement which included that the company would pay fees to H, the labour agent who would in turn pay the plaintiff. However, the company did not deal directly with H but dealt with the plaintiff. After some years, the company engaged additional six employees to work in its IT department via a similar route of using a labour agent. After a while, the plaintiff convinced both the company and the six employees to transfer the agency services to H. Thus, a written temporary service agreement was reached between the company and H in respect of the six employees. It should be noted that like the situation with the plaintiff, the company did not have direct dealings with H but engaged it through the plaintiff who facilitated the arrangement. After a while, it was discovered that unknown to both the company and the six employees, the plaintiff was receiving about 40% of the fees paid by the company to H as commission for facilitating the deal. The six employees subsequently terminated the agreement with H. The company brought an action against the plaintiff for the payment of the monies he made via the transaction which it claimed he earned in breach of his fiduciary duty to the company. The claim was dismissed by the High Court. On appeal, the contention was not that the plaintiff did not make secret profit rather that he does not stand as a fiduciary to the company. His argument was based on the fact that he had no contractual privity to the company. In upholding the appeal, the Court of Appeal held that the issue of fiduciary lies in whether in the circumstances; it would be reasonably expected of a party to act in another's interest. It held that his involvement in the transaction between H and the company was incidental to his employment as a manager in the company; and he was employed to further the interest of the company and not his personal interest. It therefore held that the plaintiff was a fiduciary who had a duty not to allow his personal interest conflict with the company's interest. The fact that he hid his commission from the company suggests that he knew he was making a secret profit.

### Directors' Fiduciary Duty in Nigeria

In Nigeria, the fiduciary position of directors is solidly codified in the Companies and Allied Matters Act.<sup>123</sup> Section 305(1) provides that directors have a fiduciary relationship with the company and shall observe utmost good faith with the company. Section 305(3) further provides that a director must always act in what he believes to be the best interest of the company. Nigerian courts have also consistently validated this statutory position. For example, in the case of *Astra Industries Nigeria Limited v. Nigerian Bank for Commerce and Industry*,<sup>124</sup> it was emphasized that

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<sup>120</sup> It is codified by the provisions of S.76(3) Companies Act 2008

<sup>121</sup> Howard Chitimira and Friedrich Hamadziripi 'A Reflective Discussion of the Director's Fiduciary Duties to the Creditors under the South African Company Law.' 2022 18 (1) *Juridica, Acta Universitatis Danubius*, 81. Available online at <https://dj.univ-danubius.ro/index.php/AUDJ/article/view/1579/2079> accessed on 10/10/2023

<sup>122</sup> (2009) 6SA 531 SCA

<sup>123</sup> Companies and Allied Matters Act 2020

<sup>124</sup> (1998) 4 NWLR (pt.145) 422 SC

acting in the best interest of the company at all times is at the core of directors' duties. Here, the issue was whether the director of the defendant bank could have exercised his discretion in favour of the plaintiff. The Supreme Court per Onu (JSC) reiterated that when a director is exercising his discretionary power, such must be exercised in the ultimate interest of the company. Similarly, in *Okeowo & Ors v. Migliore & Ors*,<sup>125</sup> the Supreme Court emphasized that the fiduciary relationship of a director with a company is not for individual benefit but rather for the benefit of the company.

It must be stated that the directors' fiduciary duty as with all other duties is owed to the company itself and not specific shareholders.<sup>126</sup> In fact, directors may take decisions which may not be favourable to the existing shareholders but which may be beneficial to future shareholders and ultimately be in the best interest of the company.<sup>127</sup> In addition, in achieving its goals of fiduciary in relation to the company, regards must be had to the needs of the employees, the consuming public, the creditors and the society as the ultimate regulator and stakeholder in company's affairs.

### The Business Judgment Rule

The 'Business Judgment Rule' was reinforced and made popular in the US case of *Re-Walt Disney Derivative Litigation*<sup>128</sup>. It is a legal doctrine which prevents a company's board from frivolous law suits based on the assumption of good faith.<sup>129</sup> The rule proposes that in the absence of contrary evidence, the actions of company's directors will not be reviewed by court because the rebuttable assumption is that they act in the best interest of the company at all times.<sup>130</sup> The rule does not necessarily clothe company directors with the garment of infallibility but believes that even in instances where they take a wrong decision, as long as there is no violation of any law or deliberate obvious act contrary to company's interest, they will be treated as exercising a business judgment in the best interest of the company but a judgment gone wrong, hence the court will not question or challenge the decisions. Thus, in suits challenging a director's action, the court in adopting the business judgment rule will uphold the decision so long as the director acted in good faith and with the belief that he was acting in the best interest of the company. The essence of the business judgment rule is to prevent or reduce pressure on directors who ordinarily exercise a lot of discretion in the discharge of their duties to the company.

It seems the earliest decision on the rule is the 1742 English case of *Charitable Corp v. Sutton*<sup>131</sup> where it was held that directors should not be held liable for good faith decisions even if such decision affected the company negatively so long as they acted diligently and with fidelity.

### Re-Walt Disney Co. Derivative Litigation:

In the United States, the case of *Percy v. Millaudon*<sup>132</sup> is the earliest decision recognizing the business judgment rule. The Supreme Court of Louisiana held that directors should not be liable for errors of judgment or mistakes if

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<sup>125</sup> More recently, the case of *NIDOCCO v. Gbajabiamila* (2013) LPELR-20899 (SC)

<sup>126</sup> Section 170(1) Companies Act 2006, see also section 305 CAMA 2020

<sup>127</sup> *Percival v. Wright* (1902) 2Ch 421, also in *Re Pantone 485 Ltd* (2002) BCLC 266 a director of two connected companies was alleged to have caused one of the companies to spend monies in excess of eighty six thousand pounds for the benefit of the other company in which he has interest, thus he caused the first company to incur a liability, the director was deemed to have breached his fiduciary duty.

<sup>128</sup> 907 A2d 693 (2005)

<sup>129</sup> *Smith v. Van Gorkom* 488 2d 858 (1985)

<sup>130</sup> *Miller v. American Telephone & Telegraph Co* 507 F.2d 759 (3<sup>rd</sup> Cir. 1974)

<sup>131</sup> *Charitable Corp v. Sutton* (1742) 26 ER 642, 2 ATK 404

<sup>132</sup> 8 Mart (n s) 68 (1829)

it was one that a prudent man can make. In *Litwin v. Allen*<sup>133</sup> the rule was expanded. It was held by the trial court that the directors of the company were liable for their decision to buy three million dollars of debentures as the purchase agreement gave the seller option to repurchase at the sale price within six months. Thus, the company bears the risk if there is a loss in value and no gain if otherwise. It was the opinion of the court that the directors in this case did not exercise their duty of care. In explaining the business judgment rule, the court made a distinction between business judgment and negligence; it stated that while directors are not liable for errors of judgment so long as they exercise reasonable skill, they are liable for negligently performing their duties.

The Walt Disney Derivative Litigation is a derivative action instituted by minority shareholders of Walt Disney Company. It was decided by the Supreme Court of Delaware and reinforces the business judgment rule. In addition, it demonstrates the application of the common law principle of minority protection. The minority shareholders of Walt Disney Company (WDC) had alleged that the directors of WDC breached their fiduciary duty in the manner of the appointment and subsequent termination of the company's President Michael Ovitz. Prior, there was a vacancy in WDC as a result of the death of its president and number two executive. The company's CEO Michael Eisner wanted a replacement and thought of Michael Ovitz who was a prominent figure in Hollywood and the founder of a successful company, Creative Artists Agency (CAA). Thus, WDC'S board appointed Ovitz with effect from October, 1995. The contract of employment was for a fixed term of five years. It contained downside protection at the instance of Ovitz who had to give up ownership of CAA to join WDC. In addition, the contract also contained clauses to the effect that if the employment was terminated before the expiration of the fixed 5 years and other than for reasons of malfeasance and gross negligence, Ovitz would receive:

- (a) His basic salary for the remaining period of the five years.
- (b)  $\frac{3}{4}$  of the annual bonus he would have received for the fixed five years.
- (c) All stocks option he would have been entitled to for the five years and
- (d) 10 million dollars in lieu of the stocks option he would have been entitled to if the contract was extended for another five years.<sup>134</sup>

The contract also contained a clause to the effect that if Ovitz left the employment other than as agreed under the contract, he would forfeit the remaining benefits under the terms of employment and will be prevented from working for a competitor.

However, by December, 1996 just slightly a year after, WDC terminated the employment but without claiming cause and therefore making Ovitz entitled to the severance package agreed in the contract and which translated to about 130 million dollars and same was paid to Ovitz. Hence, the shareholders instituted the derivative suit.<sup>135</sup> The action alleged that both the downside protection clause in the contract of employment and the eventual termination without fault<sup>136</sup> are not in the corporation's best interest; and ultimately constitute a breach of the directors' fiduciary duty.

As stated, this is a landmark case which tested two main company law principles of minority protection and the business judgment rule; thus, it lasted almost a decade, with the trial finally commencing in 2004 after a series of pre-trial motions.

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<sup>133</sup> 25 NYS 2d 667 (Sup. Ct. 1940)

<sup>134</sup> It should be stated that Ovitz had insisted on a downside protection clause because he was giving up his 55% interest in the Creative Arts Agency.

<sup>135</sup> The original complaint was dismissed by the court of chancery in *Re The Walt Disney Co Derivative Litig.* 731 A. 2d 342 (Del. Ch.1998), the dismissal was appealed against and the appellate court affirmed the dismissal in part and sustained the claim in part, yet, there were other pre-trial motions and appeals like *In Re The Walt Disney Co. Derivative Litig.* 825 A. 2d 275 Del. Ch. 2003, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000) and *In Re Walt Disney Co. Derivative Litig.* 2004 WL 2050138 (Del. Ch. 2004)

<sup>136</sup> It was alleged that there were sufficient grounds to terminate the employment for cause.

The chancery court of Delaware which was the trial court entered judgment in favour of the defendants and held the directors were not in breach of their fiduciary duty to WDC. The plaintiffs had argued that the heavy severance package constitutes a breach of fiduciary duty of the directors as it was not in the best interest of the company. Also, they contended that there was sufficient ground to terminate Ovitz' employment for fault; it was alleged among other things that Ovitz was guilty of insubordination, lying and that his general performance was subpar. The court found no evidence of lying or insubordination and held that it was immaterial that he was not as successful as expected so long as there was no proof that he was grossly negligent.<sup>137</sup>

On appeal to the Supreme Court of Delaware, the decision of the trial court was affirmed. It was contended by the appellants that the provisions on the non-fault termination in the contract of employment and the subsequent approval and payment of the severance package was a breach of duty of care and good faith by the directors and that such breach deprives them of the protection of the business judgment rule;<sup>138</sup> alternatively, it was argued that even if the business judgment rule applies, paying the severance package amounted to a corporate waste.

It was also argued against Ovitz that he breached his fiduciary duty to the company as a director because he negotiated and accepted the severance package as contained in his employment contract and also negotiated his full non fault termination payment. It was the appellants case that the trial court erred by holding that there was no breach of a fiduciary duty. The Supreme Court of Delaware in affirming the decision of the chancery court with respect to the claim against the directors decided that the appellants failed to establish any breach of duty of care or duty to act in good faith. In fact, evidence showed that the directors properly informed themselves of all material facts necessary for the employment agreement including the non-fault termination clause. Besides, there was nothing to show that Ovitz's appointment could be terminated for fault as he had not committed any malfeasance or gross negligent act. Thus, there was no way the appointment could have been terminated for cause; upholding the non-fault termination clause was the best deal the company could get in the circumstance. With regards to the alternative claim on payment of the severance package amounting to corporate waste, it was held that such claim could not stand because the company had a contractual obligation to Ovitz which it had to fulfil by the payment. Executing a contractual obligation cannot amount to a corporate waste unless the contract itself is a waste. It was the opinion of the court that the actions of the directors constituted a business judgment properly exercised and not in any way a breach of any fiduciary duty.

With respect to the claims against Ovitz, it was held that Ovitz did not have and could not breach any fiduciary duty for negotiating his contract of employment as he had not yet become an officer of the company and thus could not owe a duty.<sup>139</sup> In addition, he no longer owed a fiduciary duty after his appointment was terminated more so as he did not participate in the termination of his own appointment. The court emphasized that would be directors and former directors cannot owe a fiduciary duty. Thus, Ovitz's both pre and post appointment actions did not breach any fiduciary duty.<sup>140</sup>

As can be seen from the above, this case reinforced the principle of business judgment protection for company directors. The idea behind the rule is to solidify and validate the decision-making powers of directors, it also gives

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<sup>137</sup> While the plaintiffs tried to prove that he was negligent, there was no evidence to support such and the court rightly stated same.

<sup>138</sup> If this argument stands, it means the burden of proof will shift to Disney directors to show that they acted in good faith.

<sup>139</sup> Although, the issue of de facto presidency was argued but was rejected on the ground that it lacked both factual and legal sense besides being procedurally barred on appeal. It was held that actions that Ovitz took before his appointment took effect were incidental matters to his appointment. The alterations done to his contract of employment after his appointment did not include the issue in contention. See generally <https://casetext.com/case/in-re-walt-disney-co-derivative-litigation-2> accessed 24/10/23

<sup>140</sup> *ibid*

a basis for the exercise of their discretionary powers in managing the affairs of the company and protect them from frivolous lawsuits that can distract them from performing their duties.

A careful perusal of the rule as expounded above will in fact show that it is in itself in the best interest of the company. This is because it encourages corporate decision making and also encourages risk taking which is crucial to corporate growth and development. When directors are confident that their actions are protected as long as done in the best interest of the company, they will be more emboldened to take more risks. In the absence of solid evidence to the contrary, their decisions will always be protected as done with the best interest of the company at heart. The minority shareholders of Disney perhaps irked by public opinion and the seemingly “outrageous” amount paid to Ovitz who had barely spent a less than eventful year felt the company had been short changed and tried to “save” the company by instituting the action going all the way to the appellate stage. However, the consistency of the findings of the two courts shows the reluctance of courts to interfere in the internal workings of companies unless there is cogent reason (s) to do so; and this must be proved by the plaintiffs as evident in this case. The plaintiffs/appellants could not prove that the directors do not deserve the protection offered by the business judgment rule. It can safely be asserted that the rule in a way underscores the important roles that directors play in corporate management such that their actions are almost clothed with the toga of invisibility so long as there is no violation of a law and a breach of a fiduciary duty.

### **Business Judgment Rule in South Africa**

The rule is also recognized and codified in South Africa by virtue of section 76(4) of the Companies Act 71, 2008 which qualifies instances when the rule will apply. It provides that a director would have acted in the best interest of the company and with the degree of care, diligence and skill expected of such a director if he had taken steps to be well informed about the subject matter; the director in addition must not personally have or know someone who has personal financial interest in the subject matter of the decision<sup>141</sup> otherwise, such should be disclosed to the board of directors as required under section 75. The requirements under section 76(4) a can be explained as follows:

- a) The director (s) must have taken reasonable steps to be well informed about the subject matter.
- b) The director (s) must have no material personal financial interest or personally know a person who has personal financial interest in the subject matter of the decision otherwise, such director (s) must have disclosed same as required under section 75
- c) The director (s) must have taken such decision rationally believing same to be in the best interest of the company. This requirement is an objective one and shows why the director’s decision must not be influenced by personal interests.

In addition, section 76 (4)b provides that a director can rely on information, opinions, performance and recommendations of legal counsels, accountants and other professional advisers engaged by the company on matters of their professional competence. A director can also rely on the opinion, information, recommendation and report of employees of the company whom the directors believe are reliable and competent. A cursory look at these conditions shows that they are meant to eradicate any form of abuse or negligence and merely reinforces directors acting in good faith.

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<sup>141</sup> Section 76(4)a(ii)aa

## Business Judgment Rule in Nigeria

The Nigerian company law is essentially statutory though greatly influenced by the common law as a result of its history as a British colony. The main company legislation is the Companies and Allied Matters Act 2020. (CAMA)

The CAMA has undergone reforms from its inception as Companies Ordinance in 1912.<sup>142</sup> It has since gone through phases and amendments to reflect the needs and exigencies of the times. The Companies Act 1862 of England which was received via the Supreme Court Ordinance of 1914 made the common law, doctrines of equity and statutes of general application in force in England as at 1<sup>st</sup> January, 1900 to be applicable in Nigeria and was the earliest legislation on company law in Nigeria. Then came the Company Ordinance of 1912 which was the first local legislation and initially applicable to Lagos and later the whole country via the Companies Ordinance (Amendment and Extension) Ordinance 1917. By 1922, the Companies Ordinance 1922 came into force with amendments in 1929, 1941 and 1954. It later became the Companies Act 1963 and was in force until 1968 when it was repealed and the Companies Act 1968 came into force. The 1968 Act came with a lot of innovations and was in force until 1990 when it was repealed by the Companies and Allied Matters Act 1990 which established the Corporate Affairs Commission to administer the Act among other innovations. The 1990 Act had a number of amendments while it lasted including the 1991, 1992 and 1998 amendments. As stated, the common law is a great influence therefore a lot of common law principles have been codified.

The concept of Limited Liability Company have been codified as far back as the earliest legislation, thus, it is settled that the Companies and Allied Matters Act recognize the corporate existence of incorporated companies. It provides in sections 42 and 43 that an incorporated company is a body corporate with its own legal identity and clothed with all the powers of a natural person. This is in tandem with the common law principle of corporate personality.<sup>143</sup>

The status and importance of directors as managers of companies is also recognized under the CAMA.<sup>144</sup> It provides in section 87 that the board of directors is one of the organs that can act as the company.<sup>145</sup> It provides in (3) specifically in respect of directors that unless the articles provides otherwise, the business of a company shall be managed by the board of directors who may exercise such powers of the company that are not required by the articles of association or the Act to be exercised by the general meeting.

It goes further in (4):

*unless the articles otherwise provide, the board of directors, when acting within the powers conferred upon them by this Act or the articles, is not bound to obey the directions or instructions of the members in general meeting provided that the directors acted in good faith and with due diligence<sup>146</sup>”*

The combined effect of section 87 (1) (3) and(4) is that the Companies and Allied Matters Act recognizes that the board of directors together with the general meeting are the principal organs that acts as the company<sup>147</sup>, the board is saddled with the management of the company and is under no obligation to take instructions from the general

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<sup>142</sup> However, prior this time, it was the Joint Stock Companies Act 1855 that was the regulatory and introductory legislation on company law in Nigeria. It introduced the concept of limited liability.

<sup>143</sup> This principle was made popular by the case of *Salomon v. Salomon & Co Ltd* (1897) AC 22

<sup>144</sup> Section 269 defines a director as a person who manages and directs the affairs of a company.

<sup>145</sup> Others stated in section 87 are the general meeting, officers and agents acting under the authority of the board of directors or the general meeting.

<sup>146</sup> Emphasis is the authors.

<sup>147</sup> Officers and members in some instances when acting under the authority of the board or the general meeting can act as the company.

meeting.<sup>148</sup> In short, the board is the ultimate decision making organ of the company.<sup>149</sup> Nevertheless, 87 (5) of the Companies and Allied Matters Act provides that the general meeting can act as the board only<sup>150</sup> when the board is unable to act as a result of disqualification or a deadlock in boards' decision, but that is the only instance. The exception does not apply when the board refuses or neglects to act, in this instance, the general meeting can only institute an action on behalf of the company.<sup>151</sup> It seems therefore, that the exception allowing the general meeting to act is to forestall creating a vacuum when the board is unable to act especially as emergency situations may arise. When the failure to act is a deliberate refusal by the board, the general meeting cannot act as the board. Ultimately, the proviso in 87 (5) further entrenches the superiority of the decision-making power of the board of directors.<sup>152</sup> This assertion is supported by case law. A number of cases have described company directors as the directing mind and will of the company.<sup>153</sup>

Furthermore, the Companies and Allied Matters Act explicitly places the director in a fiduciary relationship with the company. It provides in section 305 that a director stands in a fiduciary relationship towards the company and must exercise utmost good faith in dealing with the company. It goes further in section 305 (3) and (4) to enjoin directors to always act in what it believes to be the best interest of the company. The standard is objective in ways that a normal, diligent, careful, skilful and faithful director would act in the circumstance.<sup>154</sup>

The effect of section 305 therefore is that directors' role as company fiduciaries is well grounded under the CAMA and this has been validated by case law.<sup>155</sup> In fact, no agreement or even provisions in the company's memorandum and articles of association can relieve directors of the responsibility of being a fiduciary.<sup>156</sup> It is an immutable duty<sup>157</sup>.

Having established that the CAMA recognizes the supremacy of the decision making powers of directors and also qualifies them as fiduciary to companies, the question then is are the actions of directors in Nigeria subject to judicial review when it affects the company adversely? More succinct, are their actions protected by the business judgment rule?

A look at the Nigerian case law suggests that courts are ordinarily reluctant to interfere in the internal affairs of companies.<sup>158</sup> This is more so because the CAMA recognize the proper plaintiff rule via section 341 which provides that a company is the proper plaintiff to remedy a wrong done to it or ratify an irregular conduct.

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<sup>148</sup> *Avop Plc v. Attorney General of Enugu State* (2000) 7 NWLE (Pt. 664)260 CA

<sup>149</sup> The Court of Appeal in *Batraco Limited v. Spring Bank Limited* (2015) 5NWLR (Pt. 1451) 107 CA held that the board of directors do not require authorization from the general meeting.

<sup>150</sup> For emphasis

<sup>151</sup> *Ladejobi & Ors v. Odutola Holdings Ltd & Ors* (2006) 12 NWLR (Pt. 994) CA

<sup>152</sup> Note that 87(5) also empower the general meeting to make recommendations to the board and may ratify board's decision.

<sup>153</sup> The directing mind and will idea was the dictum of Lord Denning in *H. L. Bolton (Engineering) Co. Ltd v. Graham & Sons*. Nigerian cases like *Nigerian Bank for Commerce & Industry v. Integrated Gas (Nig) Ltd* (1999) 8NWLR Pt. 613 @129; *Olawepo v. Securities and Exchange Commission* (2011) 16 NWLR (Pt. 1272) 122 CA, *Mokwe v. Ezeuko* (2000) 14NWLR (Pt.686)143 CA have followed this approach.

<sup>154</sup> They are also enjoined to have regard for the interests of the employees, the members and the environment in which the company operates.

<sup>155</sup> Curiously, section 305 (5) provides that when a director's action or decision affects a member negatively, it would not be treated as a breach of duty by the director as long as the directors' action was done in the appropriate exercise of his powers. Yet, directors should only exercises their powers for the right purpose for which it is specified.

<sup>156</sup> In fact, multiple directorships do not abrogate director's fiduciary duty.

<sup>157</sup> Secret profits, benefits and conflict of interests are prohibited. It is not an excuse that a company refused or was unable to engage in a transaction for a director to promote his personal interest.

<sup>158</sup> *Okoya & Ors v. Santili & Ors* (1990) 2 NWLR (Pt.131) 172; *Elufioye & Ors v. Halilu & Ors* (1993) 6NWLR (Pt 310)570; *Abubakri v. Smith* (1973)6 SC 31

However, section 341 is subject to some exceptions listed in 343-346 and 353 & 354. For example, section 343 empowers a member of a company to apply to court for an injunction or declaration to restrain the company and its officers from performing (a) an illegal act, (b) violating any of the provisions of the memorandum and articles of association or (c) from performing actions that will affect the personal rights of the member, (d) committing fraud, (e) in an emergency situation where a general meeting cannot be practically called, (f) where directors' will make personal profit in the transaction proposed and (g) where the interest of justice demands.

It can be argued that on the face of it, the provision of section 341 limits the exposure of the activities of directors as corporate managers to courts and judicial review, since the general rule is that it is the company itself that can remedy its wrong or ask that the court interfere and review the actions of the directors. Nevertheless, even if this analogy subsists, limiting the exposure to judicial review is different from not subjecting it to judicial review. If a court can sue/ratify wrong done to it, it means that directors actions can be reviewed by the court. A holistic interpretation of section 341 and the exceptions particularly section 343 supports that in actual fact, director's actions can be judicially reviewed. A look at the exceptions listed above especially (a), (b), (d), and (e) and (f) already qualifies as breach of fiduciary duties. When a director commits fraud against the company, the director has breached his duty to act in good faith;<sup>159</sup> the same thing when a director commits an illegal act or makes personal profit; both qualifies as breach of a fiduciary duty.

The issue then is will directors enjoy the protection offered by the business judgment rule when an action is brought challenging their actions either by the company itself or by minority shareholders through personal, representative or derivative action under Companies and Allied Matters Act?

Firstly, it can be inferred subtly from the provisions of section 305(5) but again this is limited to when the director's action negatively affects a member of the company and not when it affects the company itself. Section 305 (5) provides that a director should exercise his powers for the specified purpose and not for a collateral purpose or power and that even if it affects a member adversely, it shall not constitute a breach of duty so long as it was exercised for a proper purpose. The above provision can be regarded as subtly clothing the director with the protection of the business judgment rule when the director's action affects a member negatively.

The issue is will the same protection be available when the director's action affects the company itself negatively? The answer lies in the provision of section 738 (1) which provides:

if in any proceeding for negligence, default or breach of duty or trust against an officer of a company or a person employed by a company as auditor, it appears to the Court hearing the case that the officer or person is or may be liable but that he has acted honestly and reasonably and that, having regard to all the circumstances of the case, including those connected with his appointment he ought fairly to be excused, the Court may relieve him, either wholly or partly, from liability on such terms as it may deem fit.

A cursory look at the provisions of section 738 shows that it has solidifies the business judgement rule. It applies in situations where the company itself or a member of the company brings an action to challenge the action of a director (s). Clearly, the wordings of the section is wide to cover both an action by the company itself or that by a member of the company; it states specifically that 'in any proceeding' not limiting it to a particular kind of proceeding brought by a specific class of persons. The court is empowered to relieve such director (s) from liability if in its opinion, such director had acted honestly and reasonably irrespective of the fact that the director's action constitutes a breach of duty. This is in tandem with the spirit of the business judgment rule.

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<sup>159</sup> See *Omisade v. Akande* (1987) NGSC 11

In fact, section 738 gives a wider protection to directors in that it clothes them with anticipatory protection as they are empowered in section 738 (2) to seek relief from court in anticipation that the company or a minority shareholder may make a claim against them for negligence or breach of duty. It provides thus:

(2) when any such officer or person has reasonable apprehension that a claim may be made against him in respect of negligence, default, breach of duty or trust, he may apply to the court for relief, and the court on the application shall have the same power to relieve him as under this section it would have had if it had been a court before which proceedings against that person for negligence, default, breach of duty or trust had been brought.

It should however be noted that the provisions of section 738 is not absolute but subject to the honesty and reasonableness test.

Thus, the combined effect of the provisions of sections 305, 341, 343-346, 353, 356 and 738 of the Companies and Allied Matters Act shows that the business judgment rule is recognised under the Nigerian company legislation.

A cursory look at the Nigerian case law in this respect generally shows that while there is no express reference to the business judgement rule, courts are ordinarily reluctant to interfere in the internal affairs of the company. However, this reluctance is edged on the proper plaintiff rule as provided in section 341 stated above. For example, in *Ephraim Faloughi v. Haniel Williams & Ors*,<sup>160</sup> where a minority shareholder sought to recover company's property allegedly taken over by the director, the court held that the court will not interfere as the alleged wrong do not fall under the exceptions stated under the law. Similarly, the Supreme Court held in *Tika Tore Press Ltd v. Abina*<sup>161</sup> where following the death of a majority shareholder, directors allotted shares to themselves to gain control of the company, the administrator of the deceased shareholder sought a declaration that the allotment of shares was ultra vires, the court though agreed with the ultra vires argument but held that it was an irregularity of an internal affairs of the company which could be ratified by the company. Also, the court of appeal in *Hasal Microfinance Bank Ltd v. BDA Ltd & Anor*<sup>162</sup> reiterated the principle when it held that by the provisions of CAMA, only the board or the general meeting can authorise the institution of a suit by the company. The suit was dismissed for incompetence and abuse of court process.

### Conclusion and Recommendations

The business judgement rule developed to offer some protection to company directors against legal liability for decisions taken in the exercise of their powers as managers of the business of the company is a pro- corporate governance technique that can enhance corporate growth and development. Directors as corporate managers and fiduciaries exercise a lot of discretion in the discharge of their duties; it will not be in the ultimate interest of the company if they are handicapped from exercising their discretion optimally by the fear of liability as a result of a decision gone wrong. This is more so because of the often volatile and unpredictable business climate which can be caused by economic, political, technological and even social factors. This is perhaps why the rule has evolved over time in different jurisdictions.

This article has discussed the role of directors as managers of the affairs of companies. It in particular discussed the fiduciary role of directors with respect to companies and supports the rule that they must act in the best interest of the company at all times and discharge their responsibilities with utmost good faith. The article also examines the principle of business judgment which offers protection to directors from frivolous law suits. Specifically, the United States case of *Re Walt Disney Co. Derivative Litigation* was analysed where the business judgment rule was

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<sup>160</sup> (1978) 4F.R.C.R, 32

<sup>161</sup> (1973) LLJR, SC

<sup>162</sup> (2023) LPELR-60313(CA)

espoused richly. This article also discussed the position in South Africa and it finds that the business judgment rule has been codified in the Company's Act 71 2008 of South Africa. Then, this article analysed the Nigerian legal framework to determine the extent of the recognition and application of the business judgment rule. Specifically, the Companies and Allied Matters Act 2020 which is the main legislation on company law in Nigeria was analysed.

This article finds that while there is no express reference to the business judgment rule in the Companies and Allied Matters Act, the rule is however recognised in a number of provisions especially sections 738, 305 and 341. The article argues that the position under the Companies and Matters Act gives a wider protection to directors in Nigeria as they enjoy protection even in anticipation of possible law suits by the company or minority shareholders as the case may be.

The article therefore recommends that the business judgment rule be stretched by jurisdictions like the United States where the rule evolved and South Africa to include anticipatory relief like that stated in section 738 (2) of Companies and Allied Matters Act.

It specifically recommends that the provisions of section 76 of the South African Company's Act 71 be amended to include anticipatory relief of section 738 (2) of the Companies and Allied Matters Act.

With respect to Nigeria, it is recommended that the provision of section 305 (5) should be amended to make it clearer and unambiguous. This is to avoid possible inconsistent court judgments. While, we await legislative reforms through amendment of section 305 (5), it is recommended that the courts in Nigeria should be pro-active in the interpretation of section 305 (5), the section should be construed in concise and definite terms to capture its essence which is to offer protection to directors. This is very important as legislative reform may not be immediate. Judiciary has a key role in legal development.

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