Professional Skepticism and Corporate Transactions

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Abstract

The approval of corporate law transactions under the South African *Companies Act* 71 of 2008, as amended, is anchored in directors' standards of conduct (that is, the fiduciary duties and the duty of care, skill and diligence) as the primary requirement. It is argued that the standards of conduct of directors as a requirement for the approval of selected fundamental transactions (which require uncompromising objectivity and independence) are inadequate. Professional skepticism – a concept embedded in the work of professional auditors – is proposed as an additional standard for approval of those selected fundamental corporate law transactions. Because professional skepticism goes beyond mere objective considerations of fiduciary duties and the duty of care, skill and diligence; and requires the observance of critical factors such as having a questioning mind and making a critical assessment of transactional evidence, it is best suited for the selected fundamental transactions explained in this article, as these require a high standard of independence and transparency in their approval.

Keywords

Professional skepticism; standards of conduct of directors; fundamental corporate law transactions; financial assistance for share acquisitions; adequate consideration requirements.

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1 Introduction

At some time during the life of a company, it may need to implement any of the corporate law transactions termed fundamental transactions.[1] In this article the term "fundamental transactions" is not limited only to the three transactions that are referred to in Chapter 5 of the *Companies Act* 71 of 2008 (the *Companies Act*). The *Companies Act* classifies the following three transactions as fundamental transactions: (a) proposals to dispose of all or a greater part of the company's assets or undertaking (regulated in terms of section 112 of the *Companies Act*), (b) mergers or amalgamations (regulated in terms of section 113 of the *Companies Act*), and (c) schemes of arrangement (regulated in terms of section 113 of the *Companies Act*). This article includes financial assistance for share purchases and/or acquisitions (in terms of section 44 of the *Companies Act*) and the adequate consideration requirements for the issuance of shares (in terms of section 40 of the *Companies Act*) as fundamental transactions. Some of these transactions – such as the disposal of all or a greater part of the company's assets or undertaking or a scheme of arrangement – can be performed by the company alone,[2] while others – such as mergers or amalgamations, or financial assistance for share purchases and/or acquisitions – require the participation of other companies and/or individuals.[3]

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1 This article proposed the inclusion of two extra transactions (i.e. financial assistance for share purchases and/or acquisitions and the requirement for adequate consideration in share issuance) in what are commonly known as fundamental transactions. The main reason for their inclusion is that these transactions, too, require the exercise of uncompromising independence and objectivity as demonstrated by the statutory requirements relevant to these transactions.

2 Even though the company's asset or undertaking may amount to selling the company's subsidiary or the undertaking of its subsidiary, in general terms only a relevant company can dispose of all or greater part of its assets or undertaking; and only the relevant company can propose and implement a scheme of arrangement.

3 In the case of *City of Tshwane Metropolitan Municipality v Nambithi Technologies (Pty) Ltd* 2016 1 All SA 332 (SCA), the court emphasised the principle that in transactions where the offeror makes an offer (like a tender) and then decides to cancel the offer or abandon it, the action does not infringe on any rights and as such cannot be held liable to anybody. Conversely, merger and amalgamation transactions cannot be implemented by one company and financial assistance transactions require the participation of a potential shareholder or shareholders.

The implementation of such transactions requires strict compliance with the relevant statutory provisions of the *Companies Act*.[4] Each of these statutory requirements demonstrates the strong need for independence and objectivity, as evidenced by requirements such as the need for fair valuation,[5] the estimation of costs,[6] the retention of independent experts' reports,[7] ensuring fair and reasonable transaction terms,[8] and ensuring adequate consideration for company securities or shares.[9]

Except in situations where the statute requires the appointment of independent experts,[10] statutory compliance is the responsibility of the board of directors of the affected company.[11] Such director responsibility must be executed in accordance with original board powers, per section 66(1) of the *Companies Act,*[12] which requires the business and affairs of the company to be managed by or under the direction of its board of directors.[13] It is common cause that the execution of the board's original powers must be in line with the directors' standards of conduct, which effectively encompass fiduciary duties and the duty of care, skill and diligence.[14]

Particularly because of the inclusion of the duty to exercise independent and unfettered discretion as part of the directors' fiduciary duties at common

4 Important parts of these statutory requirements are discussed in detail in this article.

5 For example, s 112(4) of the *Companies Act* 71 of 2008 (the *Companies Act*) requires that "[a]ny part of the undertaking or assets of a company to be disposed of, as contemplated in this section, must be fairly valued as at the date of the proposal, which date must be determined in the prescribed manner."

6 Section 113(2)(h) of the *Companies Act* provides that "companies proposing to amalgamate or merge must enter into a written agreement setting out the terms and means of effecting the amalgamation or merger … setting out … the estimated cost of the proposed amalgamation or merger."

7 Section 114(2) of the *Companies Act* provides that "[t]he company must retain an independent expert … to compile a report as required by subsection (3)."

8 Both ss 44(3)(b)(ii) and 45(3)(b)(ii) of the *Companies Act* provide that "the board may not authorise any financial assistance … unless … the board is satisfied that … the terms under which the financial assistance is proposed to be given are fair and reasonable to the company."

9 In terms of s 40(1)(a) of the *Companies Act*, "[t]he board of a company may issue authorised shares only … for adequate consideration to the company, as determined by the board."

10 In terms of s 114(2) of the *Companies Act*.

11 Any of the transactions discussed in this article relate to the business and affairs of a company and those must be managed by or under the direction of the board of directors.

12 Section 66(1) of the *Companies Act*.

13 Section 66(1) of the *Companies Act*.

14 While the primary directors' standard of conduct provision is s 76(3) of the *Companies Act*, it expressly envisages the application of common law fiduciary duties by expressly requiring the exercise of directors' powers and the performance of their functions as directors of a company. When acting in that capacity they must exercise the powers and perform their functions in "good faith and for a proper purpose" (see s 76(3)(a) of the *Companies Act*).

law,[15] one may readily presume that directors' standards of conduct address compliance with the required independence and objectivity for corporate law transactions dubbed "fundamental transactions". This common law fiduciary duty, coupled with the statutory business judgment rule, may point to the need for directors' duties to be exercised with honesty, independence and objectivity.[16] However, as fiduciary duties are subject to a mixture of subjective and objective tests and the duty of care, skill and diligence is assessed objectively in accordance with a "reasonable person test", the standard is that of an ordinarily prudent person.[17] This standard is less than that of a "highly alert assessor" in accordance with the requirements of "professional skepticism". Also, because all directors' standards of conduct are underscored by the promotion of the best interests of the company, which have not been defined under the Act, the protection of the interests of other parties to fundamental transactions may not always be undertaken.

In addition to the requirements relating to directors' standards of conduct, professional skepticism requires, for example, the presence of a questioning mind and a critical assessment of transactional evidence. As professional skepticism requires the observance of standards that go beyond the mere objective requirements of directors' standards of conduct, the approval of the fundamental corporate transactions discussed in this article will be made in accordance with the highest standard of independence and meticulousness required for such transactions.

This article proceeds from the premise that the level of independence and impartiality expected in fundamental transactions is such that the current standards of conduct for directors are not fully adequate. In that context, the research question that this article attempts to answer is whether the existing opportunity for courts to develop the common law can be fulfilled through supplementing the current standards of conduct with the concept of professional skepticism in fundamental transactions. The authors acknowledge that supplementing the existing standards of conduct with the professional skepticism tool should not be interpreted as proposing the replacement of directors' standards of conduct in specified fundamental transactions. With its origin in the auditing field, the concept needs to be grounded and assimilated in the legal trajectory before it can be used to supplement the existing standards of conduct for directors. The proposal for the introduction of professional skepticism is not intended to find application

15 See, for example, *Coronation Syndicate Ltd v Lilienfeld and the New Fortuna Co Ltd* 1903 TS 489.

16 The business judgment rule is set out in s 76(4) of the *Companies Act*.

17 Observance of fiduciary duties and the duty of care, skill and diligence are generally assessed in accordance with an objective standard.

across all aspects of law which require the application of standards of directors' conduct.

1.1 Conceptual framework for professional skepticism

Professional skepticism is a very well-developed concept today, naturally observed by professional auditors in performing audits. However, there has been very little research on exactly what the concept comprises and how it could be measured.[18]

For example, in 1996 and 2000, respectively, authors such as Shaub[19] and Lawrence[20] and Choo and Tan,[21] used the concept "professional scepticism" to measure constructs such as "trust", "independence" or "suspicion". This served only to confuse "professional skepticism" with these concepts.

Today, professional skepticism is understood as "a multi-dimensional individual characteristic, encompassing both a trait (a relatively stable, enduring aspect of an individual) and also a state (a temporary condition aroused by situational variables)."[22] In that context, professional skepticism has multiple characteristics, such as a questioning mind and a propensity to assess evidence critically.[23] The full list of these characteristics, which bears testimony to professional skepticism's multi-dimensionality, consists of the following six integral components: (a) a questioning mind, (b) a suspension of judgment, (c) a search for knowledge, (d) interpersonal understanding, (e) self-esteem, and (f) autonomy.[24] To demonstrate the wider application of the concept, relatively recent research reveals its wider application in various disciplines, from auditing, psychology and philosophy to consumer behaviour.[25]

The article now turns to the six constituent characteristics of professional skepticism.

Starting with a "questioning mind", professional skepticism is arguably founded on the attitude that "includes a questioning mind".[26] This involves

18 Hurtt 2010 *Auditing* 149-150.
19 Shaub 1996 *Behavioral Research in Accounting* 154-174.
20 Lawrence 1996 *Behavioral Research in* Accounting 124-157.
21 Choo and Tan 2000 *Journal of Business Education* 72-87.
22 Hurtt 2010 *Auditing* 150.
23 Hurtt 2010 *Auditing* 151.
24 Hurtt 2010 *Auditing* 151.
25 Hurtt 2010 *Auditing* 151.
26 Statements of Auditing Standard Nos 82 and 99 of the American Institute of Certified Public Accountants (AICPA *SAS No 82*; AICPA *SAS No 99*) both indicate that professional scepticism is an attitude that "includes a questioning mind". In fact, SAS No 99 specifically increased the focus on professional scepticism as compared to previous standards by focussing on the ever-present suspicion that fraud has occurred in the preparation of the statements being audited.

"an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred."[27] This questioning mind automatically assumes the existence of fraud.[28]

Among many other accounting scholars, Nelson[29] equates scepticism with suspicion, disbelief or doubt, all of which have some aspect of this questioning construct. Research by Cozzens and Contractor;[30] Irving and Berel;[31] and Irving, DuPen and Berel,[32] among others, on media scepticism indicates that obtaining information from known sources such as friends and family increases questioning about the information obtained from unknown sources such as the media.

As for the characteristic of suspension of judgment, what is involved is the withholding judgment until there is an appropriate level of evidence upon which a conclusion can be based. The premise here is that "the auditor should not be satisfied with less than persuasive evidence."[33]

According to Mautz and Sharaf,[34] this characteristic supports the concept that judgments must be suspended until sufficient evidence is obtained. In addition, McGinn[35] states that "[t]he sceptic takes up a reflective stance compared to our ordinary practice of making and accepting knowledge claims." In the final analysis, Bunge[36] succinctly says that "[s]ceptics do not accept naively the first things they perceive or think. They are critical; they want to see evidence before believing." In this regard the suspension of judgment is the basic trait of the sceptic when confronted with dogmatic assertions.[37]

The search for knowledge as a distinct characteristic of professional skepticism differs from the characteristic of having a questioning mind because a questioning mind has some sense of disbelief or doubt, while the search for knowledge is more of a sense of general curiosity or interest.[38]

At the heart of the search for knowledge as a characteristic of professional skepticism are the following features: interest in knowledge in general and not simply to verify a specific conclusion,[39] seeking knowledge for its own

27 Hurtt 2010 *Auditing* 151.
28 Hurtt 2010 Auditing 151.
29 Nelson 2009 *Auditing* 1-34.
30 Cozzens and Contractor 1987 *Communication Research* 437-451.
31 Irving and Berel 2001 *Psychology of Women Quarterly* 103-111.
32 Irving, DuPen and Berel 1998 *Journal of Treatment and Prevention* 119-131.
33 AICPA *SAS No 82*.
34 Mautz and Sharaf *Philosophy of Auditing* 22.
35 McGinn *Sense and Certainty* 6.
36 Bunge 1991 *New Ideas in Psychology* 131.
37 See, among other, Naess *Scepticism* 5.
38 Hurtt 2010 *Auditing* 153-154.
39 Hurtt 2010 *Auditing* 153-154.

sake,[40] encouraging a desire to investigate, urging scrutiny, looking deep into and beyond the obvious, and being prepared to investigate and evaluate any new argument in relation to any questions and adopt an attitude of curiosity.

The fourth characteristic of professional skepticism is interpersonal understanding, which deals with understanding the motivation and integrity of the individuals who provide evidence.[41] The essence of the characteristic is an ability to identify the many incentives and opportunities available to client personnel to present misleading evidence or to commit fraud;[42] and to understand people's motivations and behaviours.[43]

According to Hurtt,

> Individuals' motivations and perceptions can lead them to provide inaccurate, biased, or misleading information. Unless the skeptic understands people, it is difficult to recognise the potential for bias that exists in information given by people, and it is difficult to detect when people might be intentionally providing misleading information. Once an individual's assumptions or motivations are identified and understood, the skeptic has a basis for challenging or correcting mistaken assumptions.[44]

In addition to those four characteristics of professional skepticism, research also recognises "autonomy" and self-esteem as characteristics. Exercising autonomy as a professional sceptic requires an appreciation of sceptics' power to decide for themselves regarding the level of evidence necessary to accept a particular hypothesis. Mautz and Sharaf [s]upport the need for autonomy when discussing the need for an auditor to possess professional courage. In this regard, they state "the auditor must have the professional courage not only to critically examine and perhaps discard the proposals of others, but to submit his own inventions to the same kind of detached and searching evaluations".[45] They further assert that "the prudent practitioner will take all appropriate steps to remove from his own mind any doubtful impressions or unanswered questions".[46]

McGinn identifies a sceptic as one who does not easily accept the claims of others.[47] Central to this characteristic, the sceptic needs to be able to identify the contradictions and fallacies present in the evidence or in the

40 Johnson *Skepticism and Cognitivism* 14.
41 A 2–3 of AICPA *SAS No 99*.
42 A 2–3 of AICPA *SAS No 99*.
43 See, among others, Burnyeat *Skeptical Tradition*; Hallie *Sextus Empiricus*; Johnson *Skepticism and Cognitivism*; Kurtz *New Skepticism*; McGinn *Sense and Certainty*; Popkin *History of Scepticism.*
44 Hurtt 2010 *Auditing* 154.
45 Mautz and Sharaf *Philosophy of Auditing* 136.
46 Mautz and Sharaf *Philosophy of Auditing* 136.
47 McGinn *Sense and Certainty* 6.

claims presented by others and should undertake additional investigation and evidence until he or she is personally satisfied.[48]

The last, but not least, characteristic of professional skepticism deals with self-esteem. Commentators such as Lom[49] reflect on this requisite self-esteem in terms of an inner calmness and a lack of disturbance or turmoil. While professional skepticism is originally an auditing concept, in research in the discipline of psychology self-esteem is characterised as feelings of self-worth and belief in one's own abilities.[50] The significance of self-esteem in professional skepticism has been demonstrated by research, which showed that self-esteem was found to be negatively related to persuadability[51] and negatively related to susceptibility to normative influence.[52] Authors like Boush, Friestad and Rose[53] indicate that those who are low in self-esteem lack the confidence to rely on their own judgments and suggest that self-esteem is called for to challenge persuasive attempts rather than simply to accept what is presented. Self-esteem has also been found to be positively correlated with advertising skepticism.[54]

What appears to be distinct about self-esteem is that it enables an auditor to resist attempts at persuasion and to challenge another's assumptions or conclusions.[55] According to Linn *et al*, scepticism entails some level of self-esteem that is necessary if the auditor is to take action to acquire sufficient evidence to placate the doubts or answer the questions raised during the audit itself.[56] As they argue, sceptics should possess a level of self-esteem that allows them to value their own insights at least as greatly as those of others.[57] This is an approach from which corporate law could benefit immensely.

1.2 Standards of conduct for corporate law transactions

Regardless of the unalterable requirement for shareholders to approve fundamental transactions,[58] such approval is in practice an invariable endorsement of directors' proposals, as these transactions are almost always at their (directors') initiation. Even though they are initiated by the board of directors, these transactions must be treated like any business

48 Bunge 1991 *New Ideas in Psychology* 131.
49 Lom *Limits of Doubt* 32.
50 Hurtt 2010 *Auditing* 154.
51 McGuire "Personality and Susceptibility to Social Influence" 1130-1187.
52 Clark and Goldsmith 2005 *Psychology and Marketing* 289-312.
53 Boush, Friestad and Rose 1994 *Journal of Consumer Research* 167.
54 Boush, Friestad and Rose 1994 *Journal of Consumer Research* 167.
55 Hurtt 2010 *Auditing* 155.
56 Linn, De Benedictis and Delucchi 1982 *Child Development* 1599-1613.
57 Linn, De Benedictis and Delucchi 1982 *Child Development* 1599-1613.
58 Section 115(2) of the *Companies Act* compels the approval of fundamental transactions by the shareholders through a special resolution.

decision that directors have to take in relation to their management and/or direction of the company's business and affairs. That is, as is the case in every other business decision, the directors are subject to the set standards of conduct when deciding on fundamental transactions.

Directors' standards of conduct essentially comprise fiduciary duties and the duty of care, skill and diligence. Worthington's assertion that "at a very fundamental level … these duties are directed at four well-defined objectives"[59] still rings true today. The objectives, essentially, are: to compel directors to act in accordance with the strict terms of their mandate; to compel them to exercise care and skill in carrying out their various functions; to compel them to use their wide discretionary powers in good faith and for proper purposes; and, importantly, to compel them to act loyally in advancing the interests of their companies.[60]

The four objectives of corporate directors' duties provide only a general overview of directorial duties and do not clarify the details of such duties. Notwithstanding the codification of these duties under the *Companies Act*, the exact number of the fiduciary duties applicable in South Africa is difficult to determine, as the underlying determinant of what constitutes a breach of fiduciary duty is the concept of "loyalty", honesty or good faith.[61] What is indisputable, though, is that the distinction between fiduciary duties and the duty of care, skill and diligence lies in the standard of fault required to establish liability.[62]

Directors' standards of conduct include their fiduciary duties and duties of care, skill and diligence. While we have no less than five examples of fiduciary duties[63] and a single duty of care, skill and diligence, a convincing

59 Worthington 2000 *LQR* 640.

60 Worthington 2000 *LQR* 640.

61 It is arguably incorrect to refer to the statutory position of the South African approach to directorial duties as that of "partial codification" given that the *Companies Act*'s reference to "in good faith and for a proper purpose" (under s 76(3)(a)) and the need to promote the "best interests of the company" (s 76(3)(b)) both point to the application of all common law fiduciary duties in South Africa, without exception.

62 The duty of exercising care, skill and diligence is based on both the subjective and the objective standards when it comes to care and diligence and to skills and experience, respectively. On the side of fiduciary duties, the common law applies, and it effectively imposes strict liability, as objectivity will not save the defendant in a matter of a breach of a fiduciary duty. This is because of the *sui generis* basis of a director's fiduciary duties. (See, for example, Havenga *Fiduciary Duties of Company Directors* 315; Mupangavanhu *Directors' Standards of Care.*) Also see Mongalo 2016 *Journal of Corporate and Commercial Law and Practice* 1-16; Stevens 2017 *PELJ* 20.

63 The widely accepted examples of fiduciary duties in South Africa are (a) the duty to exercise independent and unfettered discretion, (b) the duty to exercise powers for a proper purpose; (c) the duty to refrain from having their duty conflict with the company's interests, (d) the duty to refrain from taking secret profits, and (e) the duty to refrain from appropriate corporate opportunities. See among others Mongalo and

argument can be made that there are underlying "fiduciary" and "non-fiduciary" distinctions which require explicit recognition: the differentiation is between the fiduciary obligations of loyalty (i.e. obligations demanding self-denial); equitable obligations of confidence (which are not breaches of the fiduciary obligation) and equitable obligations to exercise their powers in good faith and for a proper purpose.[64]

As the basis for liability for a breach of the fiduciary duty is *sui generis*, the argument is that such liability is so wide that the duty it seeks to enforce becomes too uncertain to be adequately protected.

It may seem that the liability of directors, based on a *sui generis* concept, is uncertain and too wide. However, because of the influence of the English law, which makes use of principles derived from the law of trust, South African law developed a standard using the no profit rule in the case of *Robinson v Randfontein Estates Gold Mining Co Ltd*.[65] In this case, the court, per Innes CJ, held:

> The test is expressed, for the most part, in terms peculiar to the English law; but the principle which underlies it is not foreign to our own. For it rests upon the broad doctrine that a man, who stands in a position of trust towards another, cannot, in matters affected by that position, advance his own interests … at that other's expense.[66]

From the above, it seems that the concept of "trust" and the "promotion of the best interests of the company" (as a beneficiary of the fiduciary duties) are the standards to which to adhere when it comes to fiduciary duties. Regarding the duty of care, skill and diligence and some fiduciary duties, the standard of objectivity (anchored by the standard that negligence is a fault) and of the business judgment rule (consisting of "the no-conflict rule", the "rationality test", and the "reasonable belief") are the applicable standards.[67]

The efficacy of the directors' standards of conduct in relation to the development and authorisation of fundamental corporate law transactions is inextricably linked to the standards of trust, the promotion of the best interests of the company, the no conflict/disclosure of conflict rule, rationality and reasonable belief.

Scott *Corporate Law and Corporate Governance* 203-226. The other set of five duties similar to the above is that advocated by the Institute of Directors in South Africa (IoDSA) in their Being a Director programme, which lists the following: (a) a duty not to use one's position to gain advantage or cause harm, (b) a duty to disclose information, (c) a duty to act in good faith, (d) a duty to act in the best interests of the company, and (e) a duty to maintain confidentiality (see IODSA *Being a Director*).

64 Worthington 1999 *CLJ* 500.

65 *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 179.

66 *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 179.

67 See s 76(3)(c)(i) and (ii), read with s 76(4) of the *Companies Act*.

1.2.1 Trust

In fiduciary relationships the concept of trust defines the nature and content of the parties' interaction.[68] This concept is also used interchangeably with the concepts of good faith, loyalty and honesty.[69]

It is commonly accepted that the paramount duty of directors, individually and collectively, is to exercise their powers in good faith in the best interests of the company.[70] While at face value the duty to act in good faith in the best interests of the company simply displays subjective "good faith", it is for the director, not the courts, to consider what is in the best interests of the company. There are, of course, certain objective standards that are imposed, particularly when it must be determined whether directors have not acted with conscious dishonesty or whether they have failed to direct their minds to the question whether a transaction was in fact in the interests of the company.[71]

1.2.2 Promotion of the "best interests of the company"

What underscores directors' fiduciary duties is the promotion of the "best interests of the company". For a long time in South Africa, the question of what constitutes the "interests of the company" was unclear. Today, the influence of the constitution and the purpose clause (section 7) of the *Companies Act* points to the interests of the company being determined in line with the stakeholder inclusive approach.[72] The possibility of considering the material needs, interests and expectations of legitimate stakeholders means that the observance of this duty may present challenges to directors in terms of performing the balancing exercise in corporate decision-making. Notwithstanding the non-existent normative statement that explains what the interests of the company are,[73] the more inclusive enforcement model of the *Companies Act*,[74] coupled with the application of section 5(2) (authorising consideration of comparable foreign company law and section 7(d) (recognising the company as a means of achieving economic and

68 Havenga *Fiduciary Duties of Company Directors* 317.
69 Havenga *Fiduciary Duties of Company Directors* 332.
70 Havenga *Fiduciary Duties of Company Directors* 332.
71 Havenga *Fiduciary Duties of Company Directors* 333; Mongalo and Scott *Corporate Law and Corporate Governance* 187-226; Cassim *et al Contemporary Company Law* 683-754.
72 Although this interpretation is reflected by s 7(d) of the *Companies Act*, it is expressly reflected in principle 16 of the *King Code on Corporate Governance for South Africa* (2009) (IoDSA *King IV*).
73 As referred to in s 76(3)(b) of the *Companies Act*.
74 Exemplified by ss 157(1) and 165(2) of the *Companies Act*.

social benefits), point to the preference of a more inclusive normative statement, akin to the enlightened shareholder value approach.[75]

There should be no conflict/disclosure of conflict rule, rationality, and reasonable belief (i.e., the business judgment rule).

In determining compliance with the business judgment rule, the provisions of section 76(4) of the *Companies Act* are instructive. The subsection is known as the business judgment rule. The business judgment rule is applicable when determining whether the director has complied with the duty of care, skill and diligence and the duty to exercise his or her powers and to perform his or her functions in the best interests of the company.[76]

Factors considered in terms of the business judgment rule are (a) whether the director has taken reasonably diligent steps to become informed about the matter;[77] (b) whether the director either (i) had no material personal financial interest in the subject matter of the decision, and had no reasonable basis to know that any related person had a personal financial interest in the matter;[78] or (ii) the director complied with the requirements of section 75 with respect to any interest referred to above;[79] and (c) whether the director made a decision, or supported the decision of a committee or the board, with regard to that matter, and the director had a rational basis for believing, and did believe, that the decision was in the best interests of the company.[80]

Considerations for decision-makers in corporate transactions will encompass the above factors when their authorisations are done in accordance with the directors' standards of conduct, as they should be.

1.3 Added value of professional scepticism

The analysis of the factors considered in exercising professional skepticism and in exercising directors' standards of conduct point to some similarities and important distinctions.

While the factors to be considered in the exercise of standards of conduct are clearly spelt out by the law (either at common law or by statute) with clear parameters, those applicable for professional skepticism are not legally recognised. Given the clear legal parameters of the standards of conduct of directors, compliance with the form, rather than the spirit, may be easily resorted to. However, with professional skepticism, the fact that

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75 The enlightened shareholder value approach is legislated under s 172(1) of the United Kingdom *Companies Act*, 2006.
76 Section 76(4)(a) of the *Companies Act*.
77 Section 76(4)(a)(i) of the *Companies Act*.
78 Section 76(4)(a)(ii)(aa) of the *Companies Act*.
79 Section 76(4)(a)(ii)(bb) of the *Companies Act*.
80 Section 76(4)(a)(iii) of the *Companies Act*.

the factors important to observe are constituent parts of a person's traits and characteristics they cannot easily be faked. Furthermore, the unassailability of a questioning mind, the search for knowledge, interpersonal understanding and self-esteem – all of which are synonymous with professional skepticism – cannot be gainsaid. While other considerations of professional skepticism – such as a suspension of judgment, a search for knowledge, and autonomy – are also prevalent in directors' standards of conduct to a limited degree, they are the constituent characteristics of a professional sceptic and not of a director.

In the final analysis, standards of conduct for directors – which are inseparable from the authorisation standard of fundamental corporate law transactions – loudly call for reinforcement through some, or all, characteristics of professional skepticism.

2 Overview of the approval requirements of fundamental corporate law transactions under South Africa's corporate law

Fundamental corporate law transactions – referred to as such because of their potential impact on the change of control of the target company in favour of the bidder – are a result of business decisions for which management (as the delegate of the board of directors) is responsible.[81] A typical statutory provision demonstrating that this is the power of the board of directors is section 66(1) of the *Companies Act*, which expressly vests the power to manage and direct the business and affairs of a company in the board. As amply demonstrated in the Act, while fundamental transactions for which the board is responsible cannot be implemented without the approval of the shareholders, it is the board and not the shareholders that is responsible for proposing and putting together such transactions in the execution of the right vested in them to manage and/or direct the business and affairs of their companies. As shown in the examples of fundamental transactions below, the nature of the transactions implicated is such that without the observance of the highest standard of prudence and impartiality, the danger of those responsible acting in a self-serving and/or conflicted manner – and thus imposing what economists refer to as "agency costs" – is always present.[82] The key requirements for such transactions, as shown below, bear testimony to the need for a standard beyond just the standards of conduct of directors. The transactions are briefly explained below.

81 See s 66(1) of the *Companies Act*.
82 See Ferran *Company Law and Corporate Finance* 118.

3 Examples of corporate law transactions requiring professional skepticism

Fundamental transactions in corporate law are the focus of this article and are briefly explained in this section. The potential impact of these transactions in dispossessing some stakeholders and enriching others (sometimes unjustifiably) makes them more suitable for consideration as transactions that should be subjected to the principle of professional skepticism. Fundamental transactions are dealt with under Chapter 5 of the *Companies Act*, and can be subject to additional regulation administered by the Takeover Regulation Panel when they qualify as affected transactions, which occurs in cases where they involve regulated companies (i.e. companies with securities listed on a regulated market like the Johannesburg Stock Exchange) and are subject to Part B and C of Chapter 5 of the Act and the Takeover Regulations.

These transactions consist of (a) proposals to dispose of all or a greater part of the company's assets or undertaking,[83] (b) merger or amalgamation transactions,[84] and (c) schemes of arrangement.[85]

3.1 Proposals for the disposal of all or a greater part of the company's assets or undertaking

Section 112(2) of the Act provides that "[a] company may not dispose of all or the greater part of its assets or undertaking unless ... the disposal has been approved by a special resolution of the shareholders, in accordance with section 115; and ... the company has satisfied all other requirements set out in section 115, to the extent those requirements are applicable to such a disposal by that company."[86]

In mitigation of the risk of such a transaction being diverted to benefit those that are in control of the company (particularly the board – acting through management), the section requires that "any part of the undertaking or assets of a company to be disposed of must be fairly valued, as calculated in the prescribed manner, as at the date of the proposal."[87] While it is conceivable that most of these valuations will involve the engagement of the services of an auditor, it is not a statutory requirement that such valuations must be undertaken by auditors. From the above discussions on professional skepticism as a profession auditing is subject to professional

83 On proposals to dispose of all or a greater part of the assets or undertakings of the company, see Mongalo 2017 *SA Merc LJ* 515-526.

84 A succinct overview of mergers and amalgamation provisions is provided in Phakeng 2020 *BRICS Law Journal* 91-118.

85 Regarding schemes of arrangement as affected transactions, see Luiz 2012 *PELJ* 102-131.

86 Section 112(2) of the *Companies Act*.

87 Section 112(4) of the *Companies Act*.

skepticism, but the use of auditors cannot be compelled on the corporate decision-makers. Considering that various methods or models of valuation may produce different results, all of them may be justified on the basis that they comply with directors' standards of conduct, consisting of fiduciary duties and the duty of care, skill and diligence.

While it is not mandatory for directors, in exercising their standards of conduct, to observe professional skepticism in the determination of fair valuation in disposal transactions, the addition of professional skepticism as a requirement for these transactions would ensure the appropriately high standard of prudence and impartiality in the execution of these transactions.

It could be argued that the imposition of fair valuation requirements, on its own, should bring the level of prudence required closer to that of professional skepticism.[88] However, just because something is like professional skepticism, that does not mean that all the elements of professional skepticism can be justifiably invoked.[89]

3.2 Merger or amalgamation transactions

With regard to proposals to dispose of all or a greater part of the assets of the company or undertaking, mergers and amalgamations, envisaged under section 113 of the *Companies Act*, are subject to the risk of manipulation such that professional skepticism is not only advisable but ideal. Such a preferable state of affairs in terms of which professional skepticism should be applicable is necessitated by the terms and means of effecting merger and amalgamation agreements set out in section 113 of the *Companies Act*.[90] These terms and means of effecting a merger or an amalgamation transaction are briefly discussed below.

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88 Just as in relation to appraisal remedy, where its extension to the sales of assets – like the extension of professional scepticism to fair valuation standards - will have the effect of furthering "consistency" and reducing the consequence of form, the reality is that internal disparities between the requirements of standards of conduct and professional scepticism will show that no such consistency can operate by mere wishful thinking. Manning 1962 *Yale LJ* 258.

89 Manning, dismissing similar arguments in relation to the extension of appraisal remedy to the sale of corporate assets, maintains that the more we succeed in becoming consistent with this standard, the less consistent we become, mainly due to the fact that the pre-existing situation to which we are seeking to become "consistent" was itself internally inconsistent. See Manning 1962 *Yale LJ* 259.

90 See s 113(2) of the *Companies Act*. In particular, the relevant provisions that provide for a broad discretion of corporate decision-makers in designing these transactions are found in s 113(2)(c)-(g) and (i) of the *Companies Act*.

3.2.1 Conversion of merging or amalgamating company securities into securities of any proposed amalgamated or merged company, or exchanging them for other property

Among the terms and means of effecting a merger or an amalgamation, which must be set out in the merger or amalgamation agreement, is the following, which provided for in terms of section 113(2)(c) of the *Companies Act*. The subsection states: "companies proposing to amalgamate or merge must enter into a written agreement setting out the terms and means of effecting the amalgamation or merger and, in particular, setting out … the manner in which the securities of each amalgamating or merging company are to be converted into securities of any proposed amalgamated or merged company, or exchanged for other property."[91]

While the approval of the merger or amalgamation agreement is vested in the shareholders in terms of section 115 of the Act, the wide discretion offered to the executives and the board of companies to determine the manner in which the securities of each amalgamating or merging company are to be converted into securities of any proposed amalgamated or merged company, or exchanged for other property, needs to be directed by some standard higher than that of standards of conduct. Hence the need for professional skepticism to ensure that the much-needed independence and rigorous scrutiny of fundamental transactions is finally enabled. The standard is not intended to replace the current standards of conduct for directors. It is recommended that professional skepticism as a tool should be considered by the courts in supplementing the standards of conduct of directors currently provided for under the *Companies Act*.

Although the nuts and bolts of merger and amalgamation transactions are almost invariably the product of expert services provided by transactional advisors[92] – on the instruction of the executives and the board – the final responsibility for finalising these transactions before shareholder approval vests in the board of directors. In order to ensure the highest standard of integrity, prudence and independence, boards should not be left to their own devices in determining how the securities of merging companies are to be converted into the securities of the surviving companies or the newly incorporated companies established as a consequence of the amalgamation. Also, directors should not have a free rein to determine the nature and value of the property to be exchanged for the securities of

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91 Section 113(2)(c) of the *Companies Act*.

92 Transactional advisors, such as institutional investors, brokers, investment bankers and transactional lawyers, are the ones who usually put these mergers and amalgamation transactions into practice. These transaction advisors may include auditors, actuaries and business consultants. Their services are usually sought under the direction of corporate boards.

amalgamating or merging companies. This requires stricter oversight beyond the usual standards of conduct of directors.

3.2.2 Consideration to be received in addition to or instead of securities of any proposed amalgamated or merged company

Again, in relation to merger and amalgamation transactions, the board of directors – in the design of merger and/or amalgamation transactions – has the power to determine the consideration that the holders of securities of amalgamating or merging companies are to receive in addition to or instead of securities of any proposed amalgamated or merged company.[93]

The determination of consideration essentially involves fair valuation of the securities of amalgamating or merging companies. If money or assets equalling the value of the securities has to be paid to the holders of securities in addition to or instead of securities in any proposed amalgamated or merged company, the process of determining the fair amount to be paid and the value of the property to be exchanged for such securities has to be above reproach. If there is any conflict of interest on the part of the board members, one can rest assured that the determination of value will be questionable. However, in accordance with the standards of conduct of directors, a mere disclosure of the nature of and the circumstances relevant to the conflict will suffice as a governance response, provided the conflicted director is excluded from being part of the decision-making on the affected transactions, allowing the transaction to be approved by the remaining directors without any conflict of interest.[94] Although this may suffice for the purposes of directors' standards of conduct, the higher standard expected in terms of professional skepticism would demand more, as shown above.

3.2.3 Allocation of assets and liabilities among newly formed amalgamating companies and surviving merged companies

The allocation of assets and liabilities among newly formed amalgamating companies and surviving merged companies must be set out in the merger or amalgamation agreement.[95] This means that the board, as the decision-maker, has to fairly consider the circumstances of each of the newly formed and surviving merged companies and exercise an informed discretion on the allocation of assets and liabilities, bearing in mind the position as it existed within amalgamating or merging companies that ceased to exist or survived the merger following the implementation of the agreement. Although mergers and acquisitions are governed by an amalgamation or merger agreement (contract law principles) and the statutory merger

93 Section 113(2)(d) of the *Companies Act*.
94 The process is, for example, set out in s 75(4) and (5) of the *Companies Act*.
95 Section 113(2)(f) of the *Companies Act*.

procedure in terms of the *Companies Act*, the section still gives a wide discretion to the board to decide on the allocation of the assets and liabilities of the amalgamating or merging companies in the merger or amalgamation agreement. The decision to undertake this exercise cannot be guided by the directors' standards of conduct only, as a potential risk exists of the misallocation of assets and liabilities in terms of the resulting agreement. Therefore, it can justifiably be argued that a standard much stricter than the standards of conduct of directors is needed in such a situation. Granted, the board is most likely going to seek the professional assistance of auditors, who are subject to professional skepticism when conducting an audit. But when aiding in the allocation of assets and liabilities to newly formed amalgamated and surviving merged companies, such auditors will not be conducting an audit and they, too, cannot be said to be subject to professional skepticism in these circumstances. At any rate, the final decision on the merger or amalgamation agreement rests with the board of directors of each of the merging or amalgamating companies and they, too, are not subject to professional skepticism. The best standards shareholders and other stakeholders can rely on are the directors' standards of conduct and the professional standards of the experts hired to advise on the transaction to keep the directors in check when formulating such agreements. As a result, the call for professional skepticism in fundamental corporate transactions could not be more urgent.

3.2.4 Estimated cost of the proposed amalgamation or merger

Finally, the terms and conditions that must be set out in the merger or amalgamation agreement include those relating to the estimated cost of the proposed merger or amalgamation.[96]

Uncompromising impartiality is to be expected when the board estimates or determines the cost of the proposed merger or amalgamation. Sometimes the board may underestimate the cost of the merger so as to entice the shareholders to vote positively in favour of a particular transaction, or overestimate such costs in other situations where they want to discourage shareholders from approving the deal. The facts of the Supreme Court of Delaware case of *Paramount Communications, Inc v QVC Network, Inc*[97] demonstrate this point. In that case the facts show how the board of a target company (Paramount Communications Inc) painted a rosy picture of the cost of the merger. This was done in order to facilitate a friendly merger with Viacom Inc and to secure shareholder support. On the other hand, the board intentionally overestimated the cost of the proposed merger by an unwanted

96 Section 113(2)(h) of the *Companies Act* provides for an amalgamation or merger agreement to set out the "the estimated cost of the proposed amalgamation or merger", among other terms.

97 *Paramount Communications, Inc v QVC Network, Inc* 637 A2d 34 (Del 1994).

bidder (QVC Network Inc). The latter bid was rejected by the board, although it was a much higher bid than that of Viacom Inc.[98]

Given the risk of underestimation or overestimation of the cost of a merger or amalgamation, as demonstrated by the Delaware case above, merely relying on the directors' standards of conduct – or even the business judgment rule – would clearly be inadequate to ensure the exercise of the utmost prudence and impartiality.

3.3 Schemes of arrangement

A "scheme of arrangement" is provided for under section 114 of the *Companies Act*. It refers to a legal mechanism under South African company law which allows a company to restructure its capital or liabilities by proposing an arrangement with its shareholders or specific classes of security holders, essentially involving consolidation, division, exchange or even expropriation of securities, all requiring court approval before implementation.[99] Since the transaction involves a potential change of control through the restructuring of the company's capital or liabilities, the discretion exercised in its structuring must be free of interference.

That is exactly why the legislature has provided for the retention of an expert when schemes of arrangement are designed. In clear distinction from other fundamental transactions, section 114(2) of the Act provides for the company to retain an independent expert to compile a report, as required by subsection (3).[100] The report requires the independent expert to deal with the structure of the scheme and provide for minimum conditions, as stated in sub-sections (3)(a)-(g). To ensure independence and to encourage impartiality by the independent expert, subsection (2)(a) and (b) prescribe both competence independence and relationship independence. This is so because the first form of independence is determined by competence and experience with regard to scheme of arrangement transactions,[101] while the second form of independence is determined by the independent expert's relationship to either the company or the proponent of the scheme of arrangement.[102]

While the retention of an independent expert is a statutory requirement and is thus regulated as such, the power to appoint such an expert is vested in the board, acting on behalf of the company.[103] In the exercise of this power,

98 *Paramount Communications, Inc v QVC Network, Inc* 637 A2d 34 (Del 1994).
99 Section 114(1) of the *Companies Act*.
100 Section 114(2) of the *Companies Act*.
101 Section 114(2)(a) of the *Companies Act*.
102 Section 114(2)(b) of the *Companies Act*.
103 Section 114(2) of the *Companies Act*.

the board is subject to directorial standards of conduct.[104] It is arguable that some of the characteristics of professional skepticism are epitomised in the qualifications of an independent expert in terms of subsection (2)(a) and (b), particularly the ability to express opinions, exercise judgment and make decisions impartially.[105] However, not all the characteristics of professional skepticism are espoused by the qualifications of an independent expert. Even then, the observance of one or two of the characteristics of professional skepticism does not equal full observance of the directors' standards of conduct. That said, the professional standards with which the independent expert has to abide will provide an additional layer of protection for shareholders who are affected by the structuring of the scheme. Even if the combined effect of the independent expert's qualifications and professional standards may appear to offer something akin to professional skepticism, or even more, the lack of a statutory prescription of the profession from which the independent expert should be sourced presents a problem of inconsistency. Besides, the ultimate responsibility for the transaction remains with the board, which has only to observe directorial standards of conduct in designating the independent expert referred to in the sub-section.[106]

The imposition of professional skepticism on the board and on the independent expert as a matter of law would go a long way toward complementing directorial standards of conduct.

3.4 Financial assistance for share purchase and/or acquisition

Financial assistance for the acquisition of securities transactions under section 44 of the *Companies Act* is not classified as a fundamental transaction like the other transactions dealt with before. However, given their potential impact on the finances of the company and on the discretion accorded to directors in their execution, they deserve to be considered as candidates for the imposition of professional skepticism.

The provision of financial assistance to aid the recipient in the acquisition of the securities within a company or a company's subsidiary is a matter for regulation in accordance with shareholder contribution rules.[107] From this perspective the overriding concern in the transaction is that it should be aimed at ensuring an equitable contribution among shareholders. However, the previous approach of prohibiting and the current response to restricting

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104 Since the board's decisions regarding fundamental transactions are business decisions, they must be exercised in accordance with s 66(1) of the *Companies Act*, which authorises the board to manage or direct the management of such business decisions.

105 Section 114(2)(a)(ii) of the *Companies Act*.

106 Section 114(2) of the *Companies Act*.

107 Manning and Hanks *Legal Capital* 27, 51-66.

financial assistance appear to be based on the maintenance of capital in the interest of creditors as well as shareholders.[108] This approach tends to approach the subject from the perspective of the regulation of distribution, even though financial assistance is technically not a distribution. Discussing financial assistance for the acquisition or purchase of shares as a distribution and not a contribution is erroneous. This is because distribution relates to the payment of money or assets to the shareholders for no other reason other than on account of their being shareholders.[109] On the other hand, the potential recipients of financial assistance are as a matter of fact not yet shareholders at the time the assistance is being granted, not at least in relation to the securities for which financial assistance is being sought. Having said that, shareholder contribution rules, in terms of which financial assistance ought to be regulated, pertain to shareholders' pay-in obligations, the primary purpose of which is to ensure "equitable contribution", i.e., equal pro rata payment by security holders for securities issued by the company.[110]

While the equitable contribution to corporate coffers does not just translate into making an equal monetary contribution regardless of the period by which one becomes a shareholder in a company, one invariable feature of the "equitable contribution" rule of shareholders' pay-in obligations is that the contribution by every shareholder has to be comparable with those of other shareholders in the company, regardless of the stage at which those shareholders entered the company.[111] This is what the sections dealing with financial assistance endeavour to achieve when they insist on the need for the board to be satisfied that "the terms under which the financial assistance is proposed to be given are fair and reasonable to the company."[112]

This particular provision vests the discretion to determine the fairness and reasonableness of the terms under which financial assistance is given in the board of a company. These transactions are typically quite substantial, particularly where they relate to broad-based black economic empowerment transactions in South Africa.[113]

Given the magnitude of typical financial assistance transactions,[114] the board's prerogative to determine the fairness and reasonableness of the

108 Ferran *Company Law and Corporate Finance* 374.

109 See the definition of "distribution" in s 1 of the *Companies Act*.

110 See Manning and Hanks *Legal Capital* 51. Also see the Committee on Corporate Laws *Report on the South African Companies Act* 14.

111 Manning and Hanks *Legal Capital* 22-23.

112 See ss 44(3)(b)(ii) and 45(3)(b)(ii) of the *Companies Act*.

113 For a detailed discussion of some of the widely publicised black economic transactions, see Zim *Time and Chance* 204-299.

114 See, for example, the Western Cape High Court decision in *Trevo Capital Ltd v Steinhoff International Holdings (Pty) Ltd* (2833/2021) [2021] ZAWCHC 123 (2 July 2021) (*Steinhoff*).

terms of a financial assistance transaction appears to be quite unbridled. The discretion is, of course, subject to the satisfaction of the solvency and liquidity test by the company and, since the granting of financial assistance is a business decision, the board should also observe the directors' standards of conduct. However, the imposition of professional skepticism is recommended for these transactions in order to ensure unquestionable prudence and impartiality.

3.5 Adequate consideration requirements for the issuance of shares

The final transaction that is a suitable candidate for professional skepticism relates to the determination of the consideration for shares by directors pursuant to section 40 of the *Companies Act*. The section[115] provides boards of directors with the discretion to determine the adequacy of consideration for shares issued by the company.

This discretion of the board appears to be quite vital as its exercise may ultimately determine who actually acquires control of the company as a result of the directors' determination of the adequacy of the consideration in the company's issuance of shares. The adequacy of consideration determination by the board can be challenged only on the ground that it is not in line with directors' standards of conduct and business judgment rule in terms of section 76(3) and(4) of the *Companies Act*, read with section 77(2).[116]

Since the power of the board in respect of this crucial transaction is limited only by the directorial standards of conduct – in circumstances where a real risk exists for self-serving misconduct – the failure to extend professional skepticism to this transaction as well would not be justifiable.

4 Analysis of the application of professional skepticism to corporate law transactions

This article has argued that professional skepticism, as a standard of transactional review, presents superior qualities to the usual directorial standards of conduct characterised by fiduciary duties and the duty of care, skill and diligence.

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115 In terms of s 40(1)(a) of the *Companies Act* "[t]he board of a company may issue authorised shares only … for adequate consideration to the company, as determined by the board."

116 See s 40(3) of the *Companies Act* 71 of 2008. S 6.21(c) of the *Model Business Corporation Act*, 2022 explains this power further by stating "[t]hat determination by the board of directors is conclusive insofar as the adequacy of consideration for the issuance of shares relates to whether the shares are validly issued, fully paid, and nonassessable."

The analysis of professional skepticism demonstrates that when it comes to the exercise of discretion by those empowered to make decisions, uncompromising prudence and impartiality are of the utmost significance. In the discussion of the characteristics of professional skepticism it has been shown that the standard has matured beyond being associated with generic terms such as "trust", "confidence", and so on, to a clear technical characterisation of the intrinsic values espoused by the concept.

While this article does not argue for the abolition of the standards of conduct of directors in fundamental transactions, it maintains that such standards should operate in tandem with the professional skepticism standard if these volatile transactions are to be decided with requisite prudence and impartiality. The proposal is for this professional skepticism to be considered by the courts in applying the standards of conduct of directors in fundamental transactions, as discussed in this article. The partial codification of directors' standards of conduct in terms of section 76(3) in particular does not preclude the continued application of the common law duties of directors. The courts could therefore develop common law to fulfil the constitutional obligation.[117] The limitations of the directorial standards of conduct have been demonstrated and compared with the more independent professional skepticism.

5 Conclusion and recommendations

In conclusion, it is maintained that the fundamental transactions provided for in chapter 5 of the *Companies Act*, coupled with the significant transactions of financial assistance for the acquisition or purchase of securities in companies and the determination of the adequacy of the consideration in share issuance transactions are suitable candidates for the extension of the professional skepticism standard as set out in this article.[118]

This article does not advocate the replacement of directors' standards of conduct by the professional skepticism standard of transactional review. It recommends that at least in the above five transactions[119] the courts should supplement the directorial standards of conduct with the professional

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117 South African courts have a constitutional obligation to develop the common law in alignment with the spirit, purport, and objects of the Bill of Rights. This obligation, outlined in ss 8(3), 39(2), and 173 of the *Constitution of the Republic of South Africa*, 1996.

118 Paragraph 1.1 above.

119 These are (a) proposals for the disposal of all or a greater part of the company's assets or undertakings in terms of s 112 of the *Companies Act*, (b) mergers or amalgamations as contemplated in s 113 of the *Companies Act*, (c) schemes of arrangement as provided for under s 114 of the *Companies Act*, (d) financial assistance for share purchases or acquisition in terms of s 44 of the *Companies Act*, and directors' obligations to determine adequate consideration for the issuance of shares under s 40 of the *Companies Act*.

skepticism standard in fulfilment of their constitutional mandate to develop the common law. This article does not recommend the amendment of the *Companies Act*. It recommends that the application of standards of directors by the courts in fundamental transactions should be supplemented by the consideration of professional skepticism to promote independence and impartiality in these transactions.

While the standards of conduct of directors require the exercise of independent and unfettered discretion and the observance of business judgment, in accordance with the business judgment rule, professional skepticism, on the other hand, incorporates considerations that address important aspects of corporate law transactions such as risk assessment, fraud detection, critical evaluation, the quality of advice, reputational protection and transaction optimisation. These are in addition to accountability and compliance, which are addressed by the usual standards of conduct of directors.

The assessment of corporate law transactions reveals that the following fundamental transactions could be well regulated if their approval demanded the observance of professional skepticism. These are (a) proposals for the disposal of all or a greater part of a company's assets or undertaking, (b) merger or amalgamation transactions, (c) schemes of arrangement, (d) financial assistance for share purchases and/or acquisitions, and (e) the adequate consideration requirements for the issuance of shares.

The nature of the judgment required in the approval of these transactions arguably calls for the introduction of professional skepticism, as the current standards of conduct of directors may not be enough to ensure the much-needed impartiality and independence in these transactions.

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Companies Act, 2006

United States of America

Model Business Corporations Act, 2022

List of Abbreviations

AICPA	American Institute of Certified Public Accountants
CLJ	Cambridge Law Journal
IoDSA	Institute of Directors in South Africa
LQR	Law Quarterly Review
PELJ	Potchefstroom Electronic Law Journal
SA Merc LJ	South African Mercantile Law Journal
Yale LJ	Yale Law Journal