# DIRECTORS' STANDARD OF DUTIES OF CARE AND SKILL IN COMPANY MANAGEMENT – NIGERIAN AND ETHIOPIAN POSITIONS – AN APPRAISAL*

## *INTRODUCTION*

*Status of directors as agents of the company demands of them, in the performance of their duties, to exercise reasonable care and display such skill as they possess in the interest of the company. These duties evolved at common law, are generally less onerous than the fiduciary duties imposed by the courts of equity. This is informed by the realization that unlike a trustee of an estate who must not take risks, business ventures involve enormous risks if profits must be made. Directors therefore must not be deterred from engaging in risky ventures on behalf of their companies, provided in doing so, they acted honestly with reasonable care and skill as they possess.*

*The courts are generally unwilling to interfere in business decisions, or to substitute their own views with the views of directors reasonably held as parliament has thought it fit not to embarrass or unsettle businessmen in the performance of their vocations.*[1] *The varying degrees or qualifications of company directors coupled with different levels of company operations, make it difficult, if not impossible, for the courts to place a definite standard on the duties expected of company directors. Romer, J. aptly expressed this view in* ***Re City Equitable Fire Insurance Co***[2] *as follows;*

> *It is indeed impossible to describe the duty of directors in general terms, whether by way of analogy or otherwise. The position of a director of a company carrying on a small retail business is very different from that of a*

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* **Anthony O. Nwafor Ph.D, Assistant Professor of Law, Faculty of Law, Jimma University, Ethiopia.**

[1] See **Adebayo v Johnson & Ors** [1969] 6 NSCC 143; (1969) ANLR 171. "There is no appeal on merits from management decisions to courts of law, nor will courts of law assume to act as supervisory board over decisions within the powers of management honestly arrived at" per Lord Wilberforce in **Howard Smith Ltd v Ampol Petroleum Ltd** [1974] A.C. 821 at 832.

[2] [1925] Ch. 407 at 426.

> *director of a railway company. The duties of a bank director and the duties of director of one insurance*
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> *company may differ from those of a director of another. Thus, in determining the culpability of directors for a breach of duty, the courts usually accord paramount consideration to the knowledge and experience of the individual director whose conduct is in question.*[3]

*This subjective standard of determining directors' liability has continued to agitate academic minds and learned commentators who express strong disgust for this lowly standard of duty in modern times and with strong desire that the duty be elevated to an objective standard. The draftsman of the Nigerian Companies and Allied Matters Act*[4] *apparently expressed sympathy with this view by the provision of section 282 of the Act, but a true interpretation of that provision may not entirely attain that goal. The same view however cannot be expressed in the context of Ethiopian Commercial Code which though follows the civil law trend, is bereft of information of substance on the standard to be adopted in determining a director's culpability in the conduct of the company's affairs.*

*This work is accordingly geared at examining those provisions which reflect the current trend in the Nigerian and Ethiopian company laws on the directors' duties of care and skill.*

## DUTIES OF CARE AND SKILL – NIGERIAN PERSPECTIVE

The English court of first instance presided over by Honorable Justice Romer, in 1925 extensively reviewed the extant judicial decisions on directors duties of care and skill and came up with three propositions which have formed the basis of quantifying the extent of directors' duties of care and skill at common law.[5] Though these duties are now codified

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3. See **Re Brazilian Rubber Plantations and Estates Ltd** [1911]1 Ch.425 at 437 per Neville, J. **Lagunas Nitrate Co. v Lagunas Syndicate** [1989] 2 Ch.392 at 435 per Lindley M.R **Overend, Gurney & Co. v Gibb** (1972) L.R.5 H.L. 480 at 487-8 per Hatherley, L.C.

4. .Cap 59 Laws of the federation of Nigeria 1990 (hereinafter referred to as "CAMA" or " the Act")

5. .See **Re City Equitable Fire Insurance Co** [1925] Ch.407 at 427.

in CAMA[6] whatever improvements, if at all, made therein can only be appreciated by adopting Justice Romer's propositions as starting points.

(i). ***A director need not exhibit in the performance of his duties greater degree of skill than may reasonably be expected from a person of his knowledge and experience.***

The standard of duty required of a director by this proposition is that of a reasonable man possessing the same knowledge and experience as the director whose conduct is in question. The test thus is both objective (the standard of the reasonable man) and subjective (the reasonable man is deemed to have the knowledge and experience of the particular director).[7] This can be discerned from the decision of Neville, J. in **Re Brazilian Rubber Plantation and Estates Ltd**[8] where his Lordship accepted in principle that a director must discharge his duties with reasonable care, then proceeded to add that "such reasonable care must be measured by the care an ordinary man might be expected to take in the same circumstances on his own behalf. He is clearly... not responsible for damages occasioned by errors of judgment."[9] In an earlier case,[10] Lindley, M.R. had emphasized that;

> *If directors act within their powers, if they act with such care as is reasonable to be expected from them,* ***having regard to their knowledge and experience,*** *and if they act honestly for the benefit of the company they represent, they discharge both their equitable as well as their legal duty to the company.*

This judicial attitude stems from the realization that company directors are imbued with varying degrees of knowledge and experience. Since parliament has not deemed it fit to place any professional qualifications on the office of directors, it will be wrong to demand from a director the standard of skill or expertise which he does not possess. Thus, it has been held that a director is not bound to bring any special qualifications to his office.

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[6] See S 282 CAMA.

[7]. See Gower, L.C.B.; The Principles of Modern Company Law (3rded .) (London: Stevens & Sons 1979) at 550- 551

[8] .[1911] 1 Ch. 425.

[9] .At 437.

[10] **Legunas Nigerate Co v. Lagunas Syndicate** [1899] 2 Ch. 392 at 435. Italics supplied

> He may undertake the management of a rubber company in complete ignorance of every thing connected with rubber, without incurring responsibility for the mistakes which may result from such ignorance; while if he is acquainted with the rubber business he must give the company the advantage of his knowledge when transacting the company's business.[11]

A director of a life insurance company, for instance, does not guarantee that he has skill of an actuary or of a physician.[12] The judicial reasoning appears to be that companies having voluntarily appointed persons to the office of directors, should take them as they are. Judge Learned Hand, in an American case of **Barnes** v **Andrew**[13] buttressed this point in his answer to an argument that a director was not well suited for his job. He said; "After all it is the same corporation that chose him which now seeks to charge him. I cannot agree with the language... that in effect he implied warranty of fitness."

This lowly standard of duty demanded of directors has been subjected to highly scathing remarks by learned writers in modern times. Trebilock described it as "legacies of outmoded economic and social philosophies from another age." It amounts to judicial promotion of managerial incompetence with the resultant hardship on shareholders.[14] Professor Keeton sees it as an over indulgence by the courts to the not so competent directors.[15] Indeed to this writer, the extant judicial attitude amounts to glorification of ignorance. In other words, ignorance is a virtue while knowledge is a curse. It is rather sad that this judicial attitude has persisted in the twentieth century when corporate practice has assumed enormous complexities demanding highly managerial skill. A strong case has therefore been made for the raising of the standard of duties of care and skill expected of a director in modern times. According to Sealy,[16] there is no reason at all why the indulgence of past generations of judges towards the layman- directors of their day should continue to be enjoyed by today's highly paid professionals. And to Olawoyin,[17] the requirement that the company

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[11]. **Re Brazilian Rubber Plantation and Estate Ltd** supra at 347 per Neville J.
[12]. **Re City Equitable Insurance Co** supra. at 428 per Romer,J.
[13]. .(1924) 298 Fed 614.

[14] .Trebilock M.J.; 'The Liability of Company Directors for Negligence' (1969) 32 M.L R. 499

[15]. Keeton; 'The Directors as Trustees' (1952) 5 C.L.R. 13.
[16] 'The Director as Trustee' [1967] C.L.J. 83 at 120.
[17]. See Status and Duties of company Directors (1977) at 219.

should take its directors as they are implicit in Judge Learned Hand's decision in **Barnes' case supra** is no longer tenable in modern times where there are in existence highly qualified and experienced persons competent enough to hold the office of director. It is only natural that no one should be absorbed in a subject he does not really understand or dedicated to a post which he occupies not exactly out of interest or a profound desire to do some serious work, but perhaps merely to satisfy some sort of social gratification.

The Nigerian Law Reform commission was certainly not oblivious of these weaknesses of the common law position. Thus, in a bid to raise the standard of duty of care and skill required of a director, the Ghana's position as embodied in section 203 of Ghana's Companies Code of 1963[18] which apparently sets an objective standard of duty for directors, was considered appropriate. The Commission's recommendation is codified as section 282(1) CAMA which provides as follows;

> ***Every director of a company shall exercise the powers and discharge the duties of his office honestly in good faith and in the best interests of the company*** *and shall exercise that decree of care, diligence and skill which a reasonably prudent director would exercise* in comparable circumstances. [19]

Nigerian writers who have commented on this provision hold a unanimous view that an objective principle has been introduced in Nigerian law in substitution for the hitherto subjective standard. Osunbor for instance, has observed that "whereas the old law required a director to exercise the standard of a director of his knowledge and experience, a subjective test, the [Act] demands the standard which a reasonably prudent director would exercise in comparable circumstances, an objective test.[20] Sesegbon similarly submitted that the era of "hand of Cain, leg of Esau" approach as

[18] The section requires a director to discharge his duties to the company in such manner as a faithful, diligent, careful and ordinarily skillful director would exercise in comparable circumstances.

[19] Italics supplied. The portion in italics clearly belongs to the equitable duties of director and should not have been included in this provision.

[20] See Akanki, E.O. (ed) Essays on Company Law (1992) at 146.

expounded by Romer, J. is over because "the degree of skill and care to be shown is now that of a reasonably prudent director."[21]

It is submitted that these contentions are too presumptuous. The provision requires a director to exercise such degree of care and skill which "a reasonably prudent director would exercise in ***comparable circumstances.***"[22] Perhaps the observations of the learned writers would have been unquestionable but for the addition of the phrase **in comparable circumstances.** This creates the impression that the court is required to take into consideration factors of varying degrees in determining the liability of directors. Such factors will invariably include the knowledge and experience of the director whose conduct is in question. Davies aptly made this point where he submitted that;

> *In determining whether a director has been guilty of negligence, the court will take into account the character of the business, the number of the directors, the provisions of the articles, the ordinary course of management and practice of directors,* ***the extent of their knowledge and experience,*** *and, in short, all the special circumstances of the particular case.*[23]

Supposing we are wrong and that the court is now required to shut its eyes to the subjective knowledge and experience of the particular director whose conduct is in question, who is that "reasonably prudent director" whose knowledge and experience should be applied in determining the standard of duty expected of a director? The Act clearly offers no guide in this respect. However, it has been observed by Barnes that;

> Section 282 (1) makes it plain that a Nigerian director can no longer be regarded as an amateur. The [Act] endows him with professional status and he is compelled to accept professional standards of care as do doctors and lawyers. An objective standard has been adopted which will not yield to a directors personal circumstance.[24]

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[21] See Sasegbon, D., Nigerian Companies and Allied Matters Law and Practice (1991) at 443
[22] Italics supplied

This argument is difficult to follow. It neither arises from a natural construction of section 282 nor implicit therein that every director is now required to act as a professional. The better argument is perhaps that expressed by Osunbor who said the general standard is set somewhere in between the level of the "ignoramus or moron at one extreme and that of top flight professional director at the other extreme."[25]

It is, however, important to point out that even this latter suggestion is not a clear and impeccable deduction from the provisions of the Act. It is merely speculative and buttresses the writer's desire, and rightly held one at that, for a change in the common law position. In his comments on a similar provision under section 203 of Ghana's Companies code of 1963, Gower had observed that the provision is not intended to suddenly raise the standard, which will be unrealistic. The purpose of the provision, according to the learned author, is to enable the courts gradually evolve a standard based on an objective yard –stick in accordance with the changing trends in the business world.[26] It is on this note that Olawoyin rightly observed that any changes in the present state of the law can only be brought about by the judges and not by any attempted statutory solution,[27] which according to Dodd;[28]

> will prove extremely difficult of enforcement unless that standard is calculated to appeal to the managers themselves and thus to attain the status of a professional code of ethics rather than of a legal rule imposed upon anantagonistic group by the community at large.

This writer is of the opinion that the first step towards realizing the much desired change in the standard of duties of directors is by introducing professional qualifications for the office of a director in the statute. This issue is overdue. If secretaries of companies who in all ramifications are subordinate officers to directors are required to satisfy certain professional qualifications,[29] why not directors? This is done in the usual business life. It is not every company that appoints any person as its

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[25] Essays on Company Law op.cit. at 146-147
[26] See Report on Ghana Company Law (1961) at 145.
[27] Olawoyin, G.A.; Status and Duties of Company Director op. cit. at 228.
[28] Is Effective Enforcement of Fiduciary Duties of Corporate Managers Possible? (1934) 2 U.Chi..L Rev 194 at 199.
[29] See S.295 CAMA.

director. Certain professional qualifications or business experience are very often demanded, especially for an executive director. Statutory provisions to this effect will tremendously assist the courts in placing definite objective standard on directors on the realization that they are dealing with men of definite minimum qualification. Such provision will not be difficult to enforce as any person who assumes office as director would have known before hand what is expected of him by virtue of the office he occupies. The present negative provision which merely disqualifies certain persons from holding office as directors[30] is less than satisfactory. A bold step is required to positively prescribe minimum qualifications for directors.

**(ii). A director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodical board meetings, and at meetings of any committee of the board in which he happens to be placed .He is not, however, bound to attend all such meetings though he ought to attend whenever in the circumstances he is reasonably able to do so.**

This proposition depicts the extent of attention a director is ordinarily required to accord to the business of his company. Courts decisions in this regard are very often influenced by extraneous considerations such as reasons for the director's absence from board meetings, nature of devolution of power and number of directors. In *Re City Equitable Fire Insurance Co.*[31] where Romer, J. made this proposition, two of the directors of the company, one of whom failed to attend a board meeting for five years owing to illness, while the other was unable to attend board meetings 'regularly' because he resided and worked outside the country of operation of the company, were held not liable for losses occasioned to the company owing to mismanagement because "each one (sic) of the ... directors was willing and anxious to give of his best to the company and at all times took as active a part in the work of the board as circumstances would reasonably permit."[32]

In a much earlier case,[33] the articles had conferred supreme control and all the powers of the directors on the chairman, so that on a summons against one of the directors for misfeasance, the court absolved the director although for the four years preceding the

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[30] See SS 251,257 and 258 CAMA. See also **Prince Adebayo v Foam (Nig) Ltd** (1974) 1 FRCR 174
[31] [1925] Ch 407 See also **Re Forest of Dean Coal Mining Co** (1878) 10 Ch. 450 at 452 per Jessel M R.
[32] At 44

event he had not attended a single meeting of the directors. The court described him as " a country gentleman... not a skilled accountant being misled as he says, by reason of the extraordinary powers conferred by the articles upon [the chairman]."

Similarly in ***Re Cardiff Savings Bank, Marquis of Bute's case***[34] the Marquis of Bute succeeded his father as president of the Cardiff Savings Bank while an infant and attended only one board meeting in forty years. When the bank went into liquidator, the liquidator sought to make the Marquis liable for his neglect and omission to attend to the company's affairs which resulted in losses incurred by the bank. The court held he was not liable. Starling, J. accepted that he neglected to attend meetings, but neglect or omission to attend meetings is not... the same thing as neglect or omission of a duty which ought to be performed at those meetings."[35] In arriving at this decision, the court was impressed by the fact that there were fifty directors in the company, as such, a director who failed to attend meetings should not be held liable for the misconduct of those who attended.

A disturbing trend in this line of reasoning is the apparent promotion of indolence while punishing the vigilant. Thus, it has been said that a director who attends board meetings and rubber stamps the chairman's recommendations runs a far greater risk than one who does not attend at all.[36] Unfortunately, the provision in CAMA which is supposed to address this despicable trend also creates room for indolent directors to escape liability. Section 282(3) provides as follows:

> Each director shall be individually responsible for the actions of the board in which he participated, and the absence from the board's deliberations, ***unless justified***, shall not relieve a director of such responsibility."[37]

The active words in this provision is the phrase "unless justified." The courts decisions at common law earlier referred to clearly show that the absent directors had

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34. ( 1892) 2 Ch. 100.
[35] At 109. See also **Perry's Case** (1876) 34 L.T. 716 per Bacon V.C.

[36] See Gower's Principles of Modern Company Law 5th ed. (1992) at 587, n.28; *Selangor United Rubber Estates Lid v. Cradock* (No 3) [1968] , 1 W.L.R. 1555 at 1614.
[37] Italics supplied. Cf Art. 364(6) of Ethiopian Commercial Code discussed *infra.*

no difficulties in justifying their absence as reasons must always be found one way or the other. In his comments on the above provision, Sesegbon rightly observed that it is still possible for a director who absents himself from board's meetings and cannot attend to the affairs of the company due to his docility and laziness to justify same and thereby relieving himself of any responsibility.[38] Indeed, it is difficult to discover any changes introduced by this provision which justifies Osunbor in applauding same as salutary.[39] The inclusion of the impugned phrase in that provision literally destroys any advancement or improvement the statute is meant to make on the common law position. This may be a deliberate act aimed at sustaining the old and out-dated opinion of the Judges that directorship is a part-time occupation. In justifying this judicial approach, Keeton submitted that a businessman;

> is a busy man, and if he is, in addition, the director of several companies, then the amount of time he can devote to the affairs of any single company is of necessity very limited. Conversely, if the director is of the guinea-pig variety-if, for example, he is a distinguished nobleman with wide social and sporting activities-then his attention to business may be fleeting, and his abilities limited. Accordingly (the decisions suggest) he is not to be victimized, if the consequences of his somewhat fugitive appearances in the board-room are not always happy.[40]

Two factors emerged from this statement which are impediments to any attempt at any improvement on the present state of the law. Firstly is the concept of multiple directorship which is irreconcilable with any rule of law that may demand full attention of a director to the affairs of his company. Not even a clairvoyant exposed to the advanced modern technology can physically sit at two boards at the same time. Secondly is the absence of any statutorily prescribed qualifications for directors which creates room for a person who has little or no knowledge of the business of a company to occupy the seat of director. Invariably, such a person will exhibit less than adequate attention to a business which he has very little or no knowledge of.[41] It has earlier been shown that no step has been taken to resolve these obvious anomaly, and until such is

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[38] See Nigerian Companies and Allied Matters: Law and Practice op. cit. at 443
[39] See Essays on Company Law op. cit. at 147
[40] (1952) 5 C.L.R. 11 at 19
[41] See Olawoyin op. cit. at 222-223.

done, no effective changes can be made on the present state of the law as enforceability will be highly difficult if not impossible.

However, the provision of section 282(3), its short falls notwithstanding, may not avail an executive director who is in breach of duty. The nature of his office, coupled with his knowledge and experience in the company's business, demand from him greater attention to the affairs of the company than a non executive director. This point was buttressed by the Supreme Court in ***Adebayo v Johnson & Ors***[42] where the Court held;

> we do not think that any inherent distinction lies in the duties and liabilities of categories of directors; ***but the chairman of the Board of Directors and the Managing Director may by the Articles of Association of the company and must by the nature of their special access and conception with the detailed machinery of control be expected to know better than the other directors.***

This dictum has been codified in CAMA in section 282(4). The proviso thereof makes it clear that ''additional liability and benefit may arise under the master and servant law in the case of an executive director if there is an express or implied contract to that effect'' Thus an executive director who stays away from the board's meeting does so at his own peril.

(iii). **In respect of duties that, having regard to the exigencies of business and the articles of association, may properly be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly.**

This proposition flows from the realization that some directors of a company have greater business skill and experience than others. The law allows the directors to delegate their management powers to the more knowledgeable ones among them to execute the day to day business of the company. While exercising delegated powers, the delegates are in law agents of the company, as such, directors who delegated such

[42] (1969) 1 ANLR 171 at 192 per Coker, JSC. Italics supplied. See also Palmer's Company Law op. cit. at 932-3

powers are generally not liable for the misconduct of the managers. In ***Adebayo v Johnson & Ors***[43] the Nigerian Supreme Court held that;

> a director of a company is not expected to fill all the positions in the company himself and he should be entitled to assume that qualified staff are performing the duties of their offices with competence. He is certainly not expected to abdicate his responsibility but he is undoubtedly entitled to rely on the judgments of the responsible assistants with the requisite knowledge, training and expertise.

This decision suggests that delegation of power is not unquestionable. Two restrictions exist therein. Firstly, the delegation of power shall not amount to an abdication of duty.[44] An English Court decision in ***Dorchester Finance Co Ltd v Stebbing***[45] illustrates this point. In that case the company had three directors. One was an executive director while the other two were non-executive directors. Management was left wholly in the hands of the executive director. No board meetings were held. The non- executive directors merely paid rare visits to the company's premises. The executive director used his office to make loans to persons and companies in which he had substantial interests. These were facilitated in part by signing of blank cheques on the company's account by the non-executive directors. Foster J. held that all the three directors were liable for negligence notwithstanding that the non executive directors had acted in good faith throughout. The court rejected the defence of the non-executive directors based on non-feasance as expounded in proposition (ii) above.

In their comments on this decision, Smith and Keenan[46] submitted that the decision might have been influenced by the qualification and experience of the non-executive directors as accountants respectively which should have enabled them to dictate the fraud of the executive director. The learned authors expressed doubt on whether the

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[43] Supra at 181.See also **Dovey v Cory** [1901] A.C. 447 per Lord Halsbury L.C. at 485, per Lord Davey at 492.

[44] This is now codified in S. 279(7) CAMA. SS. 64 and 263(5) provide for delegation of powers of directors.

[45] [1989] B C L C 498. The case was decided on 22nd July 1977

[46] See Smith & Keenan's Company Law for Students (8th ed) (London: Pitman Publishing Co. 1990) at 281

same decision would be reached in the case of non-executive directors without professional qualifications or experience.

Viewed from another perspective, apart from the qualification and experience of the non-executive directors, the indolence wittingly exhibited by them to the company's affairs more than any other consideration, justifies the decision of the court. It may also be a combination of these factors. Of greater relevance however is that the decision has introduced a fairly objective standard in the quantifying of a directors duty of care as distinguished from duty of skill which is subjective. The duty of care required is that which "an ordinary man might be expected to take on his own behalf" in the running of his own business.[47] The underlying difficulty however rests in drawing a distinction between objective duty of care and subjective duty of skill. The English courts in recent times have surmounted this difficulty by having recourse to section 214(4) of Insolvency Act of 1986 which clearly sets an objective standard for determining the directors' liability for wrongful trading.[48] The courts could not see any justification why the standard of care required of a director under this provision should be different from the general duty of care and skill at common law and have thus applied the same standard in both cases.[49]

The Nigerian equivalent of this provision is section 506 CAMA which is rooted on section 213 of the English Companies Act of 1985 on fraudulent trading. Section 506 CAMA cannot be interpreted in this manner because knowledge is a prerequisite for liability under this provision.

Secondly, any delegation of duties must be made to duly qualified person. Directors will not escape liability if they consign the business of the company in the hands of incompetent manager whose conducts result in a loss to the company. The handling of a finance company must not be left to the office boy..50 In **Re City Equitable Insuranee co.'s case** , supra, one of the grounds upon which the directors were found guilty of dereliction of duty was that they left the business of the company entirely in the hands of the

47 Davies, P L. et al (ed) Gower's Principles of Modern Company Law (6th ed. 1997) at 641-642

48 See Re Produce Marketing Consortium ltd No. 2 (1989) BCLC520 where Knox J. in construing that provision held that each director had to be judged by what might reasonably be expected of a person fulfilling his functions in a reasonably diligent way.

49 See Norman v. Theodore Goddard (1991) BCLC 1027. Re D' Jan of London ltd. (1994) 1 BCLC 561

50See Gower (3rd Ed) op. cit. at 552.

managing director who usurped functions not specifically delegated to him which led to the disappearance of large amount of the company's assets out of fraud committed on the company by the managing director The company's stockbroker was also allowed to retain large sums of money without security in a manner more appropriate to bankers than to brokers, and which resulted in a loss to the company. The directors were, however, absolved from liability by a provision in the company's articles, which protected the directors in such circumstances except for willful neglect or default

It is to be noted that such exemption clause cannot be sustained under Nigerian present law. Section 67(1) CAMA has declared unequivocally that any provision in the articles or contract or otherwise, exempting an officer or any other person from liability which will otherwise attach to him due to negligence, default, or breach of trust, in relation to the company is void 51

## ETHIOPIAN PERSPECTIVE

The law regulating the operations of companies in Ethiopia is most regrettably sandwiched in a general and archaic statute referred to as the Commercial code[52] which was signed into law on the 5th day of May, 1960 by Emperor Haile Selassia I who was the then reigning monarch in Ethiopia.

The provisions relating to company operations are contained specifically in Title VI to Title IX commencing from article 304 and terminating at article 560. Suffices to observe, however, that there are references in some of these articles to provisions of other articles dealing with other subject matters within the Code which have the tendency of expanding the provisions relating to operations of companies in Ethiopia. Quite a number of these provisions are, to say the least, out dated, and have lost touch with the trend of company operations in modern times.

The provisions of the Code which are of primary relevance to us in this treatise are in article 364 which provides for liability of directors to the company in the course of the conduct of company's affairs. For the purpose of clarity, we shall set out *in extenso* the said provisions hereunder.

**Art. 364- Liability of directors to the company**

1. Directors shall be responsible for exercising the duties imposed on them by law, the memorandum or

51 See similar provision in S.310 UK CA. 1985.

52 Hereinafter referred to as "the Code"

articles of association and resolutions of meetings, **with the care due from an agent.**

2 Directors shall be jointly and severally liable to the company for damage caused by failure to carry out their duties.

3 Directors who are jointly and severally liable shall have a general duty to act with due care in relation to the general management.

4 Directors shall be jointly and severally liable **when they fail to take all steps within their power** or to mitigate acts prejudicial to the company, which are **within their knowledge.**

5 Directors shall be responsible for showing that they have exercised due care and diligence.

6 A director shall not be liable where he is not at fault and has caused a minute dissenting from the action which has been taken by the board to be entered forthwith in the directors minute book and sent to the auditors.[53]

Very close examination of these provisions in the Code reveal some interesting results on the scope of duty of care and skill imposed on directors. What is not in doubt from these provisions and some other provisions in the code is that the directors are regarded simply as agents of the company[54], and as such the quantum of duty of care required of them are merely that of an agent. The Code is completely silent on the standard of diligence which the director as such is expected to exhibit in the performance of his duties as an agent of the company. What test will the court apply in determining whether the director is in breach of his duties, should it be objective or subjective?

A comparison with the Nigerian counter part reveals the existing lacuna. Section 282(1) of CAMA provides *inter alia*;

[53] Emphasis supplied.

[54] See article 363 of the Code. But directors status are not merely that of agents, they are also organs trustees and servants of the company.

> Every director of a company shall exercise the powers and discharge the duties of his office honestly... and shall exercise that degree of care, diligence and skill which a **reasonably prudent director would exercise in comparable circumstances.**[55]

This suggests that an objective standard is intended for measuring the extent of discharge of responsibility by the director. It provides some guides on how the court can determine the culpability of a director for the breach of his duties. This guide is totally lacking under article 364 of the Code. The standard is apparently to be determined by the court at the discretion of whoever is presiding as the judge. This will continue to very from one court to another especially in this country where the system of law reporting is not synchronized. Judicial precedents are not so popular as a source of law. The shareholders who have invested in these companies and are kin on keeping watch over their investment deserve some thing better them a general statement of the existence of duty without the requisite standard.

We may , perhaps, seek guidance in the general provision contained in article 2211(1) of the Civil Code[56] which provides *inter alia;*

> The agent shall exercise the same diligence as a ***bonus pater familias*** in arrying out the agency as long as he is entrusted therewith.[57]

This provision creates the impression that the standard of care expected of an agent under Ethiopian law is that standard which the head of a family will exhibit in the running of the family business. But can this really act as a panacea to the lacuna created in article 364 of the Code having regard to the fact that that provision considers directors solely as agents of the company? Who is that ideal head of family running a business whose conduct should provide a standard for determining the extent of diligence expected of a company director. It cannot be contested that the extent of attention a man gives to his private business is governed by personal idiosyncrasy, just

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[55] Emphasis supplied. Cf. Romer, J.'s proposition (i) supra.

[56] Civil Code of the Empire of Ethiopia Proclamation No. 165 of 1960

[57] Emphasis supplied.

as it is preposterous to equate the conduct of the affairs of large public companies with that of ordinary family business. A man's attitude to his own business is certainly subjective. Should we then employ this as a standard for determining what is expected of a director of a public company?

**In Re Brazilian Rubber Plantation and Estates Ltd.** *supra* Neville J. made a judicial pronouncement akin to the provision under consideration where he said that the reasonable care expected of a director is that standard of care which "an ordinary man might be expected to take in the same circumstances on his own behalf."

The "ordinary man" in the context of article 2211(1) of the Civil Code is a family head who has no requisite business knowledge or experience but is entrusted with the running of a business empire by providence. Such a person cannot be expected to conduct the affairs of the enterprise better than his knowledge and experience can carry him. It is axiomatic that various family enterprises have been ruined due to deficiency of business knowledge and inexperience of the family heads who honestly believed they were exerting their utmost best and indeed were found to have done so when viewed subjectively. Such persons would escape liability under article 2211(1) of the Civil Code even when their best fell short of what a reasonably prudent director endowed with requisite business knowledge and experience would have done in comparable circumstances.

It is accordingly submitting that article 2211(1) of the Civil Code is not a solution to the lacuna in article 364 of the Code. The test in article 2211(1) of the Civil Code is in the main subjective, and when viewed objectively, it provides too low a standard for determining the extent of diligence which the law should demand from directors who are entrusted with other peoples investments. What is required is the standard of a director with requisite knowledge and experience running a business similar to that of the director whose conduct is in question.

An interesting dimension is brought to this argument by the provision contained in sub-article 3 of article 2211 of the Civil Code which provides inter alia;

Whosoever undertakes **without consideration** to act as an agent shall not be liable unless he has not applied to the affairs of the principal the same **degree of care as to his own**.[58]

This provision tends to draw a distinction between remunerated agents and non remunerated agents. Remunerated agents are more apposite to those class of agents dealt with under chapter 3 of the Civil Code who are described as commission agents. These are special types of agents whose functions are in the main flirting and specific, and should not be equated with company directors who though may receive remuneration when so agreed upon with the company, are more attached to the company and have very wide managerial duties. Should this provision be applied to company directors as such, it would constitute unwelcome escapade to latch unto by indolent directors whose lack of commitment inflict financial losses on the company. It would further water down the reach of the general provision in sub-article 1 of article 2211 as it constitutes an exception to the lowly element of objectivity which article 2211(1) habours. The standard of diligence expected from those class of agents envisaged in article 2211(3) is unequivocally subjective.

Sub- article 3 of article 364 does not appear to be of any relevance when read together with sub- article (1) thereof. The duties usually imposed on directors by law, memorandum of association and resolutions of the general meeting fall within the general management of the company. Provisions of article 362 of the Code buttress this fact, so that it becomes a mere surplusage to provide for a duty of care in relation to general management powers as is done under sub-article 3.

Sub–article 4 provides a very strange exculpating factor for a director who is in breach of duty by requiring that such fact which causes damage to the company must be within the knowledge of the director. In other words, the person complaining against the conduct of the director must prove that the director has knowledge of the fact resulting in damage to the company. This is an unfortunate provision, it has the potentials of destroying the essence of legal duties imposed on the directors. Knowledge is always subjective and it is always difficult to prove that some one knows except he is willing to admit that he knows.

A director will escape liability by virtue of this provision by claiming that he does not know even when such a fact has become a matter of public knowledge. The onus of proof imposed on the directors under sub- article 5, though commendable, is certainly not a panacea to the escape route offered to them by sub- article 4 of the Code.

It can also be deduced from sub- article 4 that the applicable standard for determining directors liability under article 364 is a lowly subjective standard. In this modern time and age with high wire commercial activities and quantum of other peoples resources placed under the care of directors, it is submitted that subjective standard of duty for directors is an aberration. It promotes indolence and unwittingly condones fraudulent activities in commercial transaction. This provision requires an urgent review to enact an objective standard for greater protection of the shareholders. This can be done by amending the provision to create liability where the director knows or ought to have known of the existing fact.

Sub- article 6 commendably reflects the spirit of joint and several liability of directors in the conduct of company affairs. Though directors are required to act as a board and take decisions by a majority under article 358 of the Code. A minority which did not support the decision of the majority and has actively opposed such decision which has resulted in damages to the company ought not to be held liable. There must be evidence of positive dissent, mere passivity or absence from the meeting of the board cannot be an exempting plea under this provision .

## CONCLUSION

The complexities of modern corporate organizations make it impossible for any decision of the court in relation to duties of directors to act as a binding precedent to subsequent developments. At best, they merely serve as guides, and each case is decided on its peculiar facts and surrounding circumstances. The warning of Coker J.S.C. in ***Adebayo v Johnson & ors*** is instructive in this regard, his Lordship said;

the courts must refuse to succumb to any invitation or temptation to apply the findings of fact in one case in deciding other cases of negligence or abnegation of duties in another case or other cases. 59

This warning merely re-echoed the statement of Lord Machnaghten over sixty years earlier in ***Dovey v Cory*** where his Lordship said; I do not think it desirable for any tribunal to do that which parliament has abstained from doing- that is, to formulate precise rules for the guidance or embarrassment of businessmen in the conduct of business affairs. There never has been, and I think there never will be, much difficulty in dealing with any particular case on its own facts and circumstances, and speaking for myself, I rather doubt the wisdom of attempting to do more..60

These alluring pronouncements certainly were informed by the absence of statutory provisions on duties of directors at the material times. The position has remained the same till date under the English law. But in Nigeria and Ethiopia bold steps have been taken to codify these duties. The lacunae created in these provisions will however continue to give room for divergent court decisions. More encompassing provisions are needed to reduce àreas of dissension. A close watch must however be kept on these provisions to ensure that they do not stultifying developments in company practice imbued in the societal dynamics.

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59 See supra at 180.

60 [1901] A C 447