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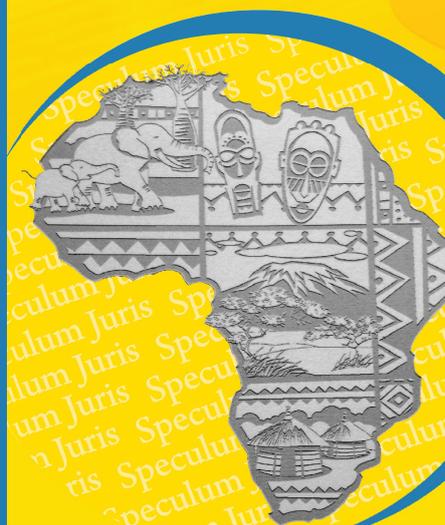


## Articles

- “Deepfakes Artificial Intelligence Generated Synthetic Media: Mapping the Revenge pornography in the South African Context”  
*by Sebo Tladi and Mpakwana Mthembu 1-21*
- “The Role of Social Welfare Policies in Advancing Socio-Economic Wellbeing and Human Rights Realisation in South Africa”  
*by Grace Mbajjorgu and Mashele Rapatsa 22-41*
- “The Water Goal: Interpreting and Linking Sustainable Development and Equity to Allow for the Realisation of Un Sustainable Development Goal 6”  
*by Muhammad Sameer Kasker 42-57*
- “Ghana’s Domestic Workers Regulations of 2020: A Critical Appraisal”  
*by Theophilus Edwin Coleman 58-80*
- “Financial Hardship as a Ground of Urgency and Foundation for Exceptional Circumstances in Applications for Interim Relief: A Review of Court Decisions”  
*by Vuyo Peach 81-97*
- “Potential Challenges Associated with Enforcing Cross-border Business Rescue Plans in the SADC Region”  
*by Kudzai Mpfu 98-115*
- “The Management Structures of Enterprises in the Southern African Financial Sector”  
*by Jeannine van de Rheede 116-139*
- “Deconstructing the Legal Framework Governing Derivatives Markets in Zimbabwe”  
*by Tariro D. Shumba and Friedrich Hamadziripi 140-161*
- “Social Crime Prevention: Why it Should be a Complementary Approach for the South African Police”  
*by Chesné Albertus and Tasné Marshall 162-184*
- “An Analysis of the Use of Chat GPT as an Unreliable Source for Legal Research by Legal Practitioners in South Africa”  
*by Patrick Mogale 185-194*
- “Strengthening the Right to Private Prosecution as an Anti-Corruption Tool in Uganda: Lessons from other Commonwealth Jurisdictions”  
*by Daniel M Walyemera 195-212*
- “Directors and AI-Assisted Decision-Making: Assessing AI’s Potential Interaction with Corporate Decision-Making Regulation Regarding Delegation, Reliance, and the Business Judgment Rule”  
*by Angella Ruth Nyasulu and Etienne Olivier 213-226*

## Notes and Comments

- “Embracing Living Customary Law: Rethinking the Teaching of African Customary Law: The case of *Mgenge v Mokoena*”  
*by Martha Keneilwe Radebe 227-240*
- “Mandatory Public Participation Before the Granting of Mining Rights: An Analysis of the Judgment in Minister of Mineral Resources and Energy and Others v Sustaining the Wild Coast NPC and Others [2024] ZASCA 84”  
*by Moses Retselisitsoe Phooko 241-252*
- “A Civil Claim Against a General Practitioner by a Child Born with Disabilities as a Result of Preconception Negligence”  
*by Magda Slabbert and Melodie Labuschaigne 253-261*
- “National Symbols, Freedom of Expression and Hate Speech: A Legal Analysis of *Afriforum NPC v Nelson Mandela Foundation Trust*”  
*by Taboko Isaac Molaba and Mpho Paulos Bapela 262-276*



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# Directors and AI-Assisted Decision-Making: Assessing AI’s Potential Interaction with Corporate Decision-Making Regulation Regarding Delegation, Reliance, and the Business Judgment Rule

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## Abstract

*Artificial intelligence (AI) has the potential to assist a company’s board of directors and enhance decision-making in companies through decreasing manual labour and increasing the efficiency with which information is processed. However, the use of AI to make decisions for a company also raises questions, such as whether and to what extent directors can rely on and delegate their responsibilities to an AI system. It is also important to establish whether the use of AI amounts to conduct that is excusable under the business judgment rule (BJR). This article measures the use of AI against the delegation, reliance, and BJR provisions in the Companies Act 71 of 2008. Since AI systems do not have legal personality in South African law, directors cannot delegate their functions to an AI system, nor rely on its advice, at least not within the contours of the Companies Act. At most, directors*

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*can use AI as a tool to process data and information more efficiently. Directors should nevertheless take reasonable steps to ensure that AI-generated advice is accurate and reliable, if necessary, by consulting professionals who can properly interpret it. The BJR can excuse AI use, provided that directors properly assess and monitor it. Unlike the United States of America (USA) and Australia, South Africa has no specific legislation or policy guidelines on the use of AI in corporate decision-making. The article reflects on American and Australian approaches to AI in corporate decision-making and argues that developing an AI governance framework for South African directors will assist them in navigating reliance on AI effectively while minimising legal risks.*

**Keywords:** Artificial intelligence; Directors; delegation; reliance; Business Judgment Rule; Companies Act 71 of 2008

## 1 INTRODUCTION

The integration of Artificial Intelligence (AI) into corporate decision-making processes represents a significant advancement in the way businesses operate. AI has the potential to assist a company's board of directors and improve decision-making in companies by decreasing manual labour and increasing the efficiency with which information is processed. However, the use of AI to make decisions for a company also presents legal challenges. For one thing, it is important to determine whether and to what extent directors can rely on, and delegate their duties to, an AI system. It is also important to establish whether the use of AI amounts to conduct that is excusable under the Business Judgment Rule (BJR).

Directors can face liability and other consequences when their conduct fails to uphold the standards of conduct specified in section 76(3) of the Companies Act 71 of 2008 (the Companies Act).<sup>1</sup> At the same time, directors are permitted to delegate specific functions and powers and rely on the advice of others.<sup>2</sup> Section 76(5) of the Companies Act affords directors protection from personal liability, provided their decisions meet the requirements of the BJR.<sup>3</sup> The article will assess how the use of AI aligns with the Companies Act's provisions on delegation and reliance, and whether the use of AI meets the standards of the BJR. The authors will also reflect on the influence of AI regarding the regulation of reliance, delegation, and the BJR in Australia and the United States of America (USA).

## 2 HOW AI CAN BE USED IN CORPORATE DECISION-MAKING

Artificial Intelligence ('AI') is considered one of the key inventions of 4IR.<sup>4</sup> Artificial Intelligence has a myriad of definitions owing to its versatile usage nature. Nevertheless, in 1956, the father and pioneer of AI, computer scientist John McCarthy, defined AI as "the science and engineering of making intelligent machines, especially intelligent computer programs."<sup>5</sup> AI uses machine learning and algorithms to autonomously learn how to process significant volumes of data and identify patterns that assist in problem-solving, decision-making or providing additional data for human evaluation.<sup>6</sup> In this context, AI can help corporate leaders in making informed

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1 See s 76(3) of the Companies Act 71 of 2008.

2 See s 76(4) of the Companies Act.

3 See s 76(5) of the Companies Act.

4 Hassani *et al.* "Artificial Intelligence (AI) or Intelligence Augmentation (IA): What is the Future? AI" 2020 *AI Journal* 145.

5 McCarthy "What is Artificial Intelligence" (2007) <http://jmc.stanford.edu/articles/whatisai.html> (accessed 18-03-2024).

6 Else and Pilegg "Corporate Directors Must Consider Impact of Artificial Intelligence for Effective Corporate Governance" (2019) *Business Law Today* published by American Bar Association 2.

decisions in the same way that it assists doctors improve diagnosis and improve patient care.

Simon once posited that “the first obvious fact about human learning is that it is horribly slow.”<sup>7</sup> He observed this in the fact that humans take six years to start school and an additional twenty years to become professionals, such as computer engineers or cognitive scientists.<sup>8</sup> Based on this, he argued that AI, through machine learning, is designed to make computers smarter through faster learning and to perform intelligent tasks that humans would otherwise need to do.<sup>9</sup> In this regard, Simon offers the perfect description of the core nature of AI: AI processes large data sets to identify patterns, thereby generating insights and predictions about future trends.<sup>10</sup> In this way, AI can help humans to make rational decisions using large data sets.<sup>11</sup> This is beneficial because the results AI provides do not come from pre-programmed rules. Rather, they are the result of a learning process (machine learning). As such, AI can become a reliable tool for directors to base their rational decision-making process on.

At its core, AI technology enables machines to replicate human skills.<sup>12</sup> Before the advent of AI, decision-makers had to make decisions manually, without technological assistance.<sup>13</sup> AI alleviates manual labour by automatically producing outputs based on provided data, unlike programmes like Microsoft Excel, where users must manually input both the data and formulae to receive results.<sup>14</sup>

A company’s board of directors must make accurate and well-informed decisions, as their errors carry higher costs compared to top management.<sup>15</sup> Directorial decisions include the recruitment and appointment of executive management, and the approval of developmental strategies.<sup>16</sup> These decisions require the board to take significant risks and assume a high level of responsibility. AI technology mitigates the risks directors face by revolutionising the way decisions are made. For instance, AI models use the Monte Carlo Simulation to minimise costs and risks in mergers and acquisitions, forecast supply and demand in the supply chain, and assess potential risks and returns in investment decisions.<sup>17</sup> AI systems are also used to collect and process client-related data, which is then analysed to improve the products and services offered by the company.<sup>18</sup> Additionally, AI helps in detecting fraudulent activities by identifying anomalies and abuse based on the customer’s transaction history.<sup>19</sup> In this process, AI undergoes machine learning, using historical transaction data that includes both legitimate and fraudulent

7 Simon “Why Should Machines Learn?” in *Machine Learning: An Artificial Intelligence Approach* (1987) 26 29.

8 *Ibid.*

9 Simon *Machine Learning* 29.

10 Shrestha, Ben-Menahem and Krogh “Organizational Decision-making Structures in the Age of Artificial Intelligence” 2019 *California Management Review* 2 3–5.

11 Rational decisions are defined as the process of selecting the choice that has the most desired outcome.

12 Jagalat *et al.* “Artificial Intelligence and Management Decisions Making: A Biometric Analysis” 2024 *IJEBMR* 35 39.

13 *Ibid.*

14 Mertens “The use of Artificial Intelligence in Corporate Decision-Making at Board Level: a Preliminary Legal Analysis” 2023 *FLIWPS* 11 14–17.

15 Nikishova and Kuznetsov *Advances in Data Mining and Database Management Book Series* (2018) 26 28–29.

16 Johri, Raval and Singh *et al.* “Big Data and Artificial Intelligence: Revolutionising Business Decision-Making” 2023 *UPCON Conference* 1692.

17 Chui “Improving Merger and Acquisition Decision-making Using Fuzzy Logic and Simulation” 2017 *IJEBM* 3 5.

18 Jarrah “Artificial Intelligence and the Future of Work: Human-AI Symbiosis in Organizational Decision Making” 2018 *BH* 583.

19 *Ibid.*

transactions.<sup>20</sup> This trains the AI model to identify abnormal and fraudulent transactions.<sup>21</sup> In this regard, AI surpasses humans in conducting complex tasks due to its advanced quantitative and analytical capabilities.<sup>22</sup> However, the best decisions require intuitive and analytical thinking.<sup>23</sup> Thus, combining human intuition and AI technology creates the ideal conditions for making business decisions, as AI provides fast data analysis while humans provide intuition.<sup>24</sup> As a result, incorporating AI into decision-making processes enables a company's board of directors to mitigate risk, enhance efficiency and minimise fraudulent activities.

### 3 AI, DELEGATION AND RELIANCE IN TERMS OF THE COMPANIES ACT 71 OF 2008

Corporate law regulations entrust directors with the management of corporate affairs and daily business operations.<sup>25</sup> However, it is often impossible for directors to perform all managerial functions and attend to all administrative functions of the company.<sup>26</sup> Therefore, it is crucial for directors to be able to delegate their powers and functions to others and rely on them to assist in fulfilling their duties.<sup>27</sup>

Delegation refers to the transfer of powers that a director is endowed with to another individual. The powers enable them to carry out tasks on behalf of the delegator for their benefit,<sup>28</sup> but reliance is defined as making decisions or acting based on information and guidance provided by an individual entrusted to deliver competent advice and guidance.<sup>29</sup>

Sections 76(4)(b) and (5) of the Companies Act offer guidelines to directors regarding how they can delegate their functions and rely on external information.<sup>30</sup> Specifically, section 76(4)(b) of the Companies Act enables directors to delegate their functions that are delegable under law to other persons.<sup>31</sup> It further enables directors to rely on the performance, information, opinions, reports and statements provided by these delegated individuals.<sup>32</sup> A director is entitled to rely on company employees whom they believe to be reliable and competent,<sup>33</sup> legal counsel, accountants or other professionals for their expertise and competence,<sup>34</sup> and board committees they are not part of, unless they have reason to doubt the committee's actions.<sup>35</sup>

Although the Companies Act does not define delegation, the case law and policy frameworks provide ample guidance on its nature and definition. The Fezile Dabi District Municipality policy framework defines delegation as "... the authorisation of a delegated power by a delegating authority to act in his stead, and in relation to a power, includes an instruction to exercise the

20 Johri *et al.* *UPCON Conference* 1690.

21 *Ibid.*

22 Johri *et al.* *UPCON Conference* 1690.

23 *Ibid.*

24 Shrestha *et al.* 2019 *CMR* 2.

25 See s 66(1) of the Companies Act 71 of 2008.

26 Goel "Delegation of Directors Powers and Duties – A Comparative Analysis" 1969 *TICLQ* 152.

27 Goel 1969 *TICLQ* 152.

28 Mupangavanhu "Delegation and Directors Reliance on the Performance of Others – A Companies Act 2008 Analysis in the Light of International Best Practices" 2023 *PELJ* 2 17–23.

29 *Ibid.*

30 Mupangavanhu 2023 *PELJ* 17–23.

31 See s 76(b)(i)-(ii) of the Companies Act.

32 See s 76(b)(i)-(ii) of the Companies Act.

33 See s 76(5)(a) of the Companies Act.

34 See s 76(5)(b) of the Companies Act.

35 See s 76(5)(a) of the Companies Act.

power or perform a function ...”<sup>36</sup> Furthermore, in the Australian case of *Huth v Clarke*, Wills J describes delegation as follows:

Delegation, as the word is generally used, does not imply a parting with powers by the person who grants the delegation, but points rather to a conferring of an authority to do things which otherwise the person would have to do himself.<sup>37</sup>

Generally, processing data, information, and performing analytical tasks on behalf of the board is a task that directors are expected to perform themselves.<sup>38</sup> When AI systems are used to process information, they perform tasks on behalf of the board.<sup>39</sup> However, AI systems do not have legal personality, therefore, they cannot, strictly speaking, be delegated duties by directors.<sup>40</sup> Instead, directors can use AI systems as a tool to fulfil their duties.<sup>41</sup> There is a crucial distinction between using AI as a tool to assist in decision-making and actual delegation. When a director uses software like Microsoft Word to draft a report for the board, this cannot be considered delegation. Rather, the director is using a tool to efficiently perform his own duties.

AI systems are given great autonomy when used to analyse data with little human input.<sup>42</sup> When directors rely on AI to process complex data, for example financial forecasts, or risk assessments, they are, in effect, abdicating an important aspect of their decision-making process.<sup>43</sup> Directors need no longer perform analytical functions themselves, but can instead rely on AI (a tool) to perform this function for them. In effect, by assigning the important task of processing data, which traditionally requires a director’s personal involvement, to an AI system,<sup>44</sup> this director has “delegated” some of his functions. However, is it truly delegation? For example, does using a search engine like Google to gather information amount to delegation? Surely not. The search engine simply aids directors in their duties without assuming any responsibilities.<sup>45</sup> Similarly, an AI system is a tool that can be used for a range of tasks, including simple ones like gathering data.<sup>46</sup> AI can also be used to perform complex analyses or make recommendations to directors. However, the use of an AI system to assist in the functions of a director still does not amount to delegation.<sup>47</sup> Currently, South African law, mainly due to the hurdle of legal personality, makes it impossible for directors to delegate their responsibilities to an AI system.

Section 76(4)(b) of the Companies Act provides that duties may be reasonably delegated to persons.<sup>48</sup> According to section 1 of the Companies Act, a “person” also includes a juristic

36 Fezile Dabi District Municipality “Chapter 1: Policy Framework for Delegation of Powers and Functions” <https://feziledabi.gov.za/wp-content/uploads/2022/03/chapter-1-delegations-policy-framwork.pdf> (accessed 19-08-2024).

37 *Huth v Clarke* (1890) 25 QBD 391 para 391.

38 See s 76 of the Companies Act.

39 Johri *et al.* 2023 *UPCON Conference* 12.

40 Jingchenn “Artificial Intelligence and Corporate Decisions: Fantasy, Reality or Destiny” 2022 *CULR* 695.

41 Laher “Why AI a Tool Aand Not A Replacement for Human Originality” <https://www.forbes.com/councils/forbesbusinessdevelopmentcouncil/2023/05/26/why-ai-is-a-tool-and-not-a-replacement-for-human-originality/> (accessed 19-10-2024).

42 Johri *et al.* 2023 *UPCON Conference* 1690.

43 Shrestha *et al.* 2019 *CMR* 4 2.

44 Goel 1969 *TICLQ* 152.

45 Google “Explore the World of Google Searc” <https://www.google.com/search/howsearchworks/> (accessed 18-10-2024).

46 *Ibid.*

47 Goel 1969 *TICLQ* 152.

48 See s 76(4)(b) of the Companies Act.

person, such as a company.<sup>49</sup> An AI system is fundamentally a computer software system.<sup>50</sup> It is neither a natural person nor a juristic person. AI systems lack the legal personality required to assume fiduciary duties and responsibilities as humans do.<sup>51</sup> Considering these factors, directors cannot delegate any of their functions to AI systems.

Directors often rely on third parties to fulfil their duties prudently.<sup>52</sup> Section 76(4)(b) of the Companies Act states that a director may rely on certain individuals or groups when performing his/her duties, provided that the director has a reasonable basis for the reliance.<sup>53</sup> Section 76(5) of the Companies Act specifies that a director is entitled to rely on company employees and the information provided by them, if the director reasonably believes these employees are reliable and competent; professional advisors, such as legal counsel and accountants, if the director reasonably believes they have the necessary expertise and are trustworthy; and board committees, even those the director is not a member of, unless there is reason to doubt the committee's actions.<sup>54</sup>

The Companies Act allows directors to rely on professionals only if they reasonably trust their competence.<sup>55</sup> Reasonable reliance is a legal concept explaining how “a prudent person would believe, and act based on information provided by another party.”<sup>56</sup> To better understand the nature of reasonable reliance, it is important to consider contract law principles that clarify how reasonable reliance operates. In the contractual dispute case, *Slip Knot Investments v Du Toit*,<sup>57</sup> Kruger J stated that reliance is reasonable where it was appropriate for one party to depend on the actions or statements of another party, considering the surrounding circumstances and the expected level of expertise and understanding.<sup>58</sup> This understanding of reasonable reliance is consistent with common law *dicta* explaining a director's role in relation to reliance. In *Fisheries Development Corporation of SA Ltd v Jorgensen*,<sup>59</sup> the court held that directors may not passively rely on information and advice; they must give due consideration to all information and ultimately exercise their own judgement considering the information provided.<sup>60</sup>

Directors can legitimately rely on information and advice provided by AI systems to make decisions, but only to the extent permitted by sections 76(4)(b) and 76(5) of the Companies Act.<sup>61</sup> Due to its lack of legal personality, an AI system cannot fall under the categories of company employees, professional advisors, or board committees that a director can rely on for information and advice.<sup>62</sup> However, directors can use AI indirectly through an expert who uses it to gather information that the director uses to ultimately make a decision. Prior to deciding, a director is required to give due consideration and exercise their own judgement when applying

49 See s 1 of the Companies Act.

50 Marshall “No Legal Personhood for AI” 2023 *Patterns* 1 2–3.

51 Jingchenn 2022 *CULR* 663 668.

52 Cassim “A Critical and Comparative Analysis of Delegation and Reliance by Company Directors under the South African Companies Act 71 of 2008” 2024 *AICL* 125 128–135.

53 See s 76(5) Companies Act.

54 See s 76(5)(a)–(c) of the Companies Act.

55 See s 76(5)(a)–(c) of the Companies Act.

56 Cornell School of Law “Reasonable Reliance” [https://www.law.cornell.edu/wex/reasonable\\_reliance#:~:text=Reasonable%20reliance%20is%20a%20legal,involving%20the%20tort%20of%20fraud](https://www.law.cornell.edu/wex/reasonable_reliance#:~:text=Reasonable%20reliance%20is%20a%20legal,involving%20the%20tort%20of%20fraud) (accessed 22-08-2024).

57 *Slip Knot Investments 777 (Pty) Ltd v Du Toit* 2010 ZASCA 34.

58 *Slip Knot Investments 777 (Pty) Ltd v Du Toit* 2010 ZASCA 34 paras 7–13.

59 *Fisheries Development Corporation of SA's case* 535.

60 *Fisheries Development Corporation of SA Ltd v Jorgensen and Another; Fisheries Corporation of SA Ltd v AWJ Investments (PTY) LTD and others* 1980 4 All SA 525 (W) 535.

61 See s 76(4)(b) and s 76(5) of the Companies Act.

62 See s 76(5)(a)–(c) of the Companies Act.

the AI-generated information in the decision-making process.<sup>63</sup> These reliance principles are designed to prevent directors from blindly following third-party advice, including AI outputs, and ensure that any reliance is based on informed judgement and proper verification.<sup>64</sup>

Directors must be prudent when relying on the advice generated by AI systems to make decisions. Reasonable reliance would be established by directors who assess whether it is appropriate for them to depend on the information provided by the AI system. This determination would depend on the expertise of AI developers or data scientists responsible for the system's programming and function. Experts who use AI systems should ensure that the information utilised to make the decision has been processed in a manner that aligns with the board's duty of care. This requires experts to verify that the AI system processes data accurately and appropriately and can thus provide reliable insights that directors can reasonably rely on to make informed decisions. As such, directors must also have reasonable belief in the competence of the experts who oversee and use the AI systems.

While tools such as ChatGPT are available to directors for direct use, their usage does not remove the need for expert oversight. The use of easily accessible AI tools, such as ChatGPT, to make business-related decisions exposes the company to significant risks. A programme such as ChatGPT is not tailored for business advice and may cause risks such as inaccurate, outdated information, and data privacy breaches. Therefore, directors need to work in conjunction with experts when relying on AI systems, as the lack of such oversight could expose directors to legal and fiduciary risks. If directors take reasonable steps to ensure that AI-generated advice is accurate and reliable, by consulting professionals who can properly interpret it, they should be within the bounds of the Companies Act when relying on AI systems.

In Australian law, directors are allowed to rely on information provided by competent employees, professional advisors, experts, and committees.<sup>65</sup> However, there is no explicit reference to AI in the Corporations Act. Despite this, the Australian Institute of Company Directors ("AICD"), in partnership with the Human Technology Institute, has released guidelines to assist directors in using AI tools.<sup>66</sup> Although these guidelines do not carry legal force, they serve as a practical framework to help directors align their use of AI with existing duties under the Corporations Act.<sup>67</sup> The guidelines also emphasise the importance of setting up proper governance frameworks. For example, the AICD guidelines advise directors to take necessary steps in establishing governance frameworks and oversight mechanisms to effectively rely on AI systems.<sup>68</sup> In establishing a governance structure, directors must assess whether the board is adequately equipped to oversee AI use.<sup>69</sup> This may include establishing new committees solely dedicated to AI use or adapting existing committees, such as risk committees, to include AI oversight.<sup>70</sup> It may also require integrating external AI experts or forming a panel of experts to provide directors with ongoing guidance and insights into AI developments.<sup>71</sup> Most importantly, the AICD guides directors to adopt flexible governance systems that are tailored to the specific context of their organisation.<sup>72</sup> By following these guidelines, directors can ensure

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63 *Fisheries Development Corporation of SA's case 535.*

64 *Cassim 2024 AICL 125 128–135.*

65 See ss 189(a)(i)–(iv) of the Corporations Act 2001.

66 Australian Institute of Directors "A Director's Introduction to AI" <https://www.aicd.com.au/content/dam/aicd/pdf/tools-resources/director-resources/a-directors-introduction-to-ai-web.pdf> (accessed 31-08-2024).

67 *Ibid.*

68 *Ibid.*

69 Australian Institute of Directors "A Director's Introduction to AI".

70 *Ibid.*

71 *Ibid.*

72 *Ibid.*

that AI-generated information is relied on responsibly.

South Africa leaves directors without structured guidelines on AI use. This leaves directors exposed to uncertainty and risk when relying on AI systems to make decisions.<sup>73</sup> The emergence of AI use in corporate governance makes it important for South Africa to consider adapting its reliance framework. While Australian law is not inherently different from South African law in terms of reliance principles, the existence of AI-specific guidelines in Australia provides directors a clearer path for safely integrating AI into decision-making.<sup>74</sup> In contrast, South African law lacks similar direction, which leaves directors exposed to greater uncertainty and potential legal risks when relying on AI systems.<sup>75</sup> South Africa can use this as an opportunity to consider implementing similar guidance, possibly through the Institute of Directors South Africa or the Companies and Intellectual Property Commission ('CIPC'), or another regulatory body, by issuing a Practice Note or a Guidance document. By developing an AI governance framework for directors, such as the AICD guidelines,<sup>76</sup> South Africa could provide its directors with tools to navigate reliance on AI effectively while minimising legal risks. This would ensure that the reliance on AI systems is in accordance with the directors' duties and responsibilities under the Companies Act.<sup>77</sup>

#### 4 AI AND THE BUSINESS JUDGEMENT RULE IN TERMS OF THE COMPANIES ACT 71 OF 2008

The BJR is encapsulated in section 76(4) of the Companies Act, which provides that the rule applies where the director "took reasonably diligent steps to become informed about the matter; had no material personal financial interest in the matter ...; and made or supported a decision with a rational basis for believing it was in the best interests of the company."<sup>78</sup> The BJR is a liability standard by which courts review the decisions of the board of directors.<sup>79</sup> This rule has been argued to function as both an abstention and immunity doctrine.<sup>80</sup> Bainbridge argues that it is more appropriate to view the BJR as an abstention doctrine because it limits courts from reviewing directors' decisions unless specific conditions are met.<sup>81</sup> As such, the rule creates a strong rebuttable presumption that directors' decisions are made with due care, placing a significant burden on the plaintiff to overcome that presumption.<sup>82</sup> Conversely, viewed through the lens of the immunity doctrine, the BJR is seen as a tool that grants directors immunity,

73 Stamford "Gartner Identifies Six ChatGPT Risks Legal and Compliance Leaders Must Evaluate" <https://www.gartner.com/en/newsroom/press-releases/2023-05-18-gartner-identifies-six-chatgpt-risks-legal-and-compliance-must-evaluate> (accessed 10-10-2024).

74 See ss 189(a)(i)–(iv) of the Corporations Act.

75 Hamadziripi *et al.* "The Integration and Reliance on Technology to Enhance the Independence and Accountability of Company Directors in South Africa" 2020 *PELJ* 20.

76 Australian Institute of Directors "A Director's Introduction to AI".

77 See ss 76(4)(b) and 76(5) of the Companies Act.

78 See ss 76(4)(a)(i)–(ii) of the Companies Act.

79 Bainbridge "The Business Judgement Rule as Abstention Doctrine" 2004 *VLR* 83 88–90. This abstention approach continues to be influential and has been supported by more recent scholarship, such as Velasco "A Defence of the Business Judgment Rule" 2020 *Journal of Corporation Law* 647, 660–665, which reinforces the need for judicial deference to board autonomy to preserve managerial discretion.

80 McMillan "The Business Judgement Rule as an Immunity Doctrine" 2013 *William & Mary Business Law Review* 56 58–60 and Sharfman "The Importance of the Business Judgment Rule" 2017 *New York University Journal of Law and Business* 14 27–31.

81 Velasco 2020 *JCL* 661.

82 *Ibid.*

shielding them from liability for business decisions.<sup>83</sup>

In addition to the protections that the rule offers, the contours and requirements of the BJR provide directors with clarity on making informed decisions, particularly when delegating duties and relying on third parties to attend to duties. Directors who delegate and rely on information and advice provided by others are expected to do so responsibly, ensuring that the delegated parties are competent and that the information relied upon is credible. The BJR supports this by allowing directors to effectively manage their responsibilities while being assured that their well-founded decisions are legally protected.<sup>84</sup> Overall, the rule aims to make sure that directors remain accountable and to safeguard the interests of shareholders from abuse of power.<sup>85</sup>

Section 76(4)(a) of the Companies Act outlines the circumstances under which a director will have fulfilled the duties outlined in sections 76(3)(b) and (c) of the Companies Act (the duties of exercising powers in the company's best interests and with appropriate care, skill, and diligence).<sup>86</sup> Section 76(4)(a) of the Companies Act provides that the duties are fulfilled where the director has taken reasonably diligent steps to be informed about the matter,<sup>87</sup> has no material personal financial interest in the subject matter of the decision,<sup>88</sup> and believed that the decision was in the best interests of the company on a rational basis.<sup>89</sup>

Regarding the first requirement of section 76(4)(a)(i), the Companies Act does not provide guidance concerning what qualifies as "reasonably diligent steps to become informed about the matter."<sup>90</sup> To determine what this entails, courts consider the general principles of reasonableness and the specific context in which the director was operating.<sup>91</sup> The criterion of reasonableness considers the *boni mores* of the community, and the director's conduct is required to align with that of a reasonable person.<sup>92</sup> Therefore, in evaluating a director's actions, it is determined whether the director took steps that a reasonable person, in the same position, would have taken to become informed.<sup>93</sup> Other contextual considerations that are also taken into account are as follows: (1) their access to information, where failure to obtain information is considered as less diligent; (2) directors with more expertise and experience are expected to use that foundation to analyse and gather information more thoroughly; and (3) full-time directors may be expected to take more comprehensive steps to gather information than part-time non-executive directors.<sup>94</sup>

Turning to the second requirement of the statutory BJR, a director should not have a material personal financial interest in the subject matter of the decision.<sup>95</sup> According to section 1 of the Companies Act, a personal financial interest is material where it is significant enough to affect the director's judgement.<sup>96</sup> Finally, regarding the last requirement, as established in *Visser*

83 McMillan 2013 *William & Mary Business LR* 69.

84 Branson "A Business Judgement Rule for Incorporating Jurisdictions in Asia?" 2011 *SACJLJ* 691 693.

85 *Ibid.*

86 See s 76(3)(b) and (c) of the Companies Act.

87 See s 76(4)(a)(i) of the Companies Act.

88 See s 76(4)(a)(ii) of the Companies Act.

89 See s 76(4)(a)(iii) of the Companies Act.

90 See s 76(4)(a) of the Companies Act.

91 Muswaka "Shielding Directors Against Liability Imputations: The Business Judgement Rule and Good Corporate Governance" 2013 *Spec J* 29 30–32. Also see Passador "Governance Gambits and Business Judgment in In/Out-Sourcing Tactics" 2024 *ABLJ* 5–7.

92 *Coronation Brick (Pty) Ltd v Strachan Construction Co (Pty) Ltd* 1982 4 SA 371 (D) para 338.

93 *Cede & Co v Technicolor Inc.* 634 A.2d 1993 345 para 14.

94 Muswaka 2013 *Spec J* 29.

95 *Ibid.*

96 See s 1 of the Companies Act.

*Sitrus (Pty) Ltd and Goede Hoop Sitrus (Pty) Ltd*,<sup>97</sup> a rational decision is defined as one that aligns with the purpose for which the director is authorised to make the decision.<sup>98</sup> Although present in corporate law, the concept of rationality shares similarities across legal fields. Under administrative law, rationality requires that decisions must be based on reason.<sup>99</sup> In this regard, reason includes some of the following considerations: the purpose for which the decision was made; reasons provided for the decision; and the information considered when the decision was being made.<sup>100</sup> This determination contains an element of subjectivity, considering the special expertise and experience of the decision-maker.<sup>101</sup> In *Democratic Alliance v President of South Africa*, the court held that rationality has a single, consistent standard and applies uniformly in legal contexts.<sup>102</sup> This case illustrates that the legal principles underlying rationality within administrative law can also be applied in corporate law. As such, under the BJR, a decision can also be considered rational if the director has made an informed decision with a genuine purpose, considering their expertise and experience, and can provide a clear reason for the decision.

The BJR acknowledges that human beings are fallible and recognises that directors have limited computational skills and memory.<sup>103</sup> As such, the BJR provides a legal framework protecting directors from liability when delegating tasks or relying on third-party advice or information.<sup>104</sup> Where all the requirements of the statutory BJR are met, directors will be protected from liability for losses that the company has incurred due to decisions made in good faith (even if those decisions yield extensive losses and general bad results). In addition, the rule guides directors on the requirements they need to meet to successfully meet their duty of care, skill, and diligence.<sup>105</sup>

Directors must maintain good business judgement by ensuring that they are reasonably informed, have no personal financial interest in a decision, and believe that the decision serves the best interests of the company.<sup>106</sup> AI systems can significantly enhance business judgement.<sup>107</sup> Relying on AI systems could enhance directors' ability to make more informed decisions.<sup>108</sup> This could reduce the directors' subjectivity and improve their business judgement and decision-making abilities.<sup>109</sup> The capabilities of AI systems allow directors to access adequate information prior to making decisions.<sup>110</sup> AI systems can assist directors in collecting, formatting, collating, distributing, and regularly updating data when compiling periodic reports that reflect the true state of the business.<sup>111</sup> Reports compiled in such a way would help directors make more

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97 *Visser Sitrus (Pty) Ltd v Goede Hoop Sitrus (Pty) Ltd and Others* 2014 5 SA 179 (WCC).

98 *Ibid* para 77.

99 Brynard "Justifying Administrative Action for Reasonableness: A Quest for Accountable Public Administration" 2013 *Administratio Publica* 69 72–73.

100 Brynard 2013 *Administratio Publica* 72.

101 *Ibid*.

102 *Democratic Alliance v President of South Africa and Others* 1 SA 248 (CC) para 44.

103 Bainbridge 2004 *VLR* 121.

104 *Ibid*.

105 See s 76(4) of the Companies Act.

106 *Ibid*.

107 Jagalat *et al.* 2024 *IJEBMR* 39.

108 Zhao "Artificial Intelligence and Corporate Decisions: Fantasy, Reality or Destiny" 2022 *CULR* 68.

109 *Ibid*.

110 Zhao 2022 *CULR* 68.

111 *Ibid*.

informed and higher-quality decisions.

Directors frequently struggle to consider all relevant corporate governance principles and extensive literature before making decisions, largely due to time constraints.<sup>112</sup> South African directors can make more independent and accountable decisions by using augmented AI systems<sup>113</sup> and data analytics, which provide advanced computing and analysis power.<sup>114</sup> For instance, to improve their independence and accountability, South African directors can use IBM Watson's cognitive computing systems, a powerful digital technology solution.<sup>115</sup> Watson functions with or without an internet connection and enables directors to interact using images, text, and voice commands. The Swedish Standard Bank is an example of a company that uses this system to handle customer enquiries.<sup>116</sup> These capabilities can also grant stakeholders and shareholders access to minutes, annual general meetings, and real-time updates on the company's affairs. The system integrates vast amounts of data, processing it into unbiased information for decision-making.<sup>117</sup> AI programmes like Watson provide directors with essential information for well-informed, objective decisions by producing unbiased outputs.<sup>118</sup> The use of AI systems in decision-making would thus enable directors to apply the principles of the BJR more effectively to safeguard their business decisions.

The use of AI in decision-making raises questions about how the BJR applies when directors depend on AI systems. Beyond ensuring the quality of directors' decision-making, the BJR shields directors from liability.<sup>119</sup> However, the BJR only protects decisions made with adequate knowledge and understanding. On the face of it, the BJR is crucial because it prevents directors from requiring constant shareholder approval and prevents courts from imposing their own ideas of what constitutes sound business practice.<sup>120</sup>

The use of AI amounts to conduct that is excusable by the BJR, even if it causes loss. As discussed previously, directors cannot delegate duties to AI systems and can only rely on AI when it is used to compile information by experts. Therefore, the BJR can only be used as a defence by directors when relying on AI if they fulfil the abovementioned requirements set out in section 76(4)(a)(i) to (iii) of the Companies Act.<sup>121</sup> In fact, using AI can strengthen their chances of successfully using the BJR, as AI improves the quality of business judgements and helps directors make informed decisions.<sup>122</sup> AI assists directors in making more objective decisions that are free from personal financial interests and align with the company's best interests.<sup>123</sup> However, if directors do not properly assess and monitor AI usage through AI experts, their

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112 Zhao 2022 *CULR* 68.

113 Advisory (or augmented) AI operates autonomously and can create scenarios and simulations. It also engages complex problem-solving and decision-making by answering and asking questions. It also enhances human intelligence by providing guidance and information that would otherwise be difficult or time-consuming to obtain (Petrin "Corporate Management in the Age of AI" 2020 *CBLR* 985).

114 Hamadziripi *et al.* 2020 *PELJ* 25.

115 *Ibid.*

116 Hamadziripi *et al.* 2020 *PELJ* 20.

117 *Ibid.*

118 Hamadziripi *et al.* 2020 *PELJ* 22.

119 *Ibid.*

120 Cowger "Corporate Fiduciary Duty in the Age of Algorithms" 2022 *Journal Law, Technology and the Internet* 153.

121 See s 76(4)(a)(i) of the Companies Act.

122 See s 76(4)(a)(i) of the Companies Act.

123 See s 76(4)(a)(ii) to (iii) of the Companies Act.

reliance on AI could be considered negligence, leading to loss of protection from the BJR.

Although there are strong arguments for applying the BJR to AI-assisted decisions, significant challenges remain. Cowger has criticised these arguments, asserting that the BJR should not apply when fiduciaries rely on AI systems.<sup>124</sup> He contends that AI-based decisions lack adequate knowledge and, as a result, cannot be considered informed judgements.<sup>125</sup> In the American case of *Smith v Van Gorkom*, the court held that directors who make their decisions based on “an unintelligent or unadvised judgement” cannot be entitled to BJR protection.<sup>126</sup> Based on this statement, Cowger argues that decisions made based on AI advice might not consider all material information, as directors might not fully grasp how AI algorithms process data or the potential biases in the data.<sup>127</sup> As a result, these decisions may not be fully informed, which conflicts with section 76(4)(a)(i) of the Companies Act.<sup>128</sup> While Cowger’s concerns are valid, directors can reasonably rely on AI by collaborating with AI experts to ensure the accuracy of information used in decision-making. This approach effectively addresses the issues raised by Cowger.<sup>129</sup>

In the United States of America (USA), courts are generally reluctant to hold directors liable for unsuccessful business decisions stemming from bad judgement.<sup>130</sup> American judges typically defer to board decision-making, recognising that directors, as “business experts”, are better suited to assess business risks.<sup>131</sup> Therefore, unless a board breaches its fiduciary duties, American courts generally refrain from second-guessing the substance of a director’s business decisions or risk assessments.<sup>132</sup>

In response to the rising use of AI systems, the United States has introduced several federal laws, such as the National Artificial Intelligence Initiative Act of 2020<sup>133</sup> and the AI in Government Act.<sup>134</sup> These federal laws guide directors on what to consider when incorporating AI in decision-making.<sup>135</sup> The USA has also introduced various regulations to ensure transparency,<sup>136</sup> protection from discrimination,<sup>137</sup> and accountability<sup>138</sup> when using AI systems. In 2023, The White House Office of Science and Technology Policy issued a Blueprint for an AI Bill of Rights that

124 Cowger 2023 *JLTI* 153.

125 *Ibid.*

126 *Smith v Van Gorkom* 488 A.2d 858, 872 (Del. 1985).

127 Cowger 2023 *JLTI* 153.

128 See s 76(4)(a)(i) of the Companies Act.

129 Cowger 2023 *JLTI* 153.

130 Bainbridge 2004 *VLR* 89.

131 *Dodge v Ford Motor Co* 170 N.W. 668, 684 (Mich. 1919).

132 Sharfman “The Importance of the Business Judgement Rule” 2017 *New York University Journal of Law & Business* 46.

133 See the National Artificial Intelligence Initiative Act of 2020.

134 See the AI in Government Act of 2020.

135 Szczepański “United States Approach to Artificial Intelligence” 2023 [https://www.europarl.europa.eu/RegData/etudes/ATAG/2024/757605/EPRS\\_ATA\(2024\)757605\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/ATAG/2024/757605/EPRS_ATA(2024)757605_EN.pdf) (accessed 05-09-2024).

136 The states of California, Maryland, Illinois and New York City enacted legislation that requires companies to disclose when they’re using AI for customers to be aware of its use. For example, consent may be required by an employee prior to the company processing employee data using AI systems. (Wright “Artificial Intelligence in the States: Emerging Legislation” 2023 <https://www.csg.org/2023/12/06/artificial-intelligence-in-the-states-emerging-legislation/> (accessed 05-09-2024).

137 The states of Illinois, California and Colorado enacted legislation to prevent AI systems from contributing to discrimination based on race, disability or sex, amongst others. Through this regulation, the state requires developers to assess systems for potential bias before deploying them. *Ibid.*

138 The states of Delaware, California and Connecticut, amongst other states, have enacted legislation that holds those developing and deploying AI systems accountable for failure to abide by standards that govern AI systems. (Wright “Artificial Intelligence in the States: Emerging Legislation”).

echoes the same principles.<sup>139</sup> This policy outlines guiding principles for AI, ensuring that AI systems are safe, transparent, explainable, non-discriminatory, protect people from abusive data practices, and provide alternatives for human decision-making.<sup>140</sup> Aside from these regulations, like Australia, the United States has not yet enacted corporate law legislation specifically governing the use of AI in decision-making and corporate governance.<sup>141</sup> Nevertheless, existing laws provide guidance on what they should consider when employing such tools when making business judgements.<sup>142</sup> In the American context, for directors to successfully make good business judgements and use BJR as a defence mechanism when employing AI, they must ensure that they are fully informed.<sup>143</sup> This entails that directors must be transparent, accountable and avoid any form of discrimination in their use of the data processed by AI and in the decision-making process. Additionally, directors must ensure that the AI systems rely on accurate and reliable information that is free from bias.<sup>144</sup> Furthermore, directors must exercise due care by understanding how AI systems operate to meet the legal standards outlined in federal laws.<sup>145</sup>

In South Africa, the National Artificial Intelligence Policy Framework introduces principles of fairness, accountability, transparency, and inclusivity to build trust and mitigate risks such as bias and discrimination.<sup>146</sup> Although South Africa has yet to implement policies or laws specifically guiding directors on how to use AI in decision-making, introducing similar frameworks to the ones in the United States could provide the required guidance for directors relying on AI systems.<sup>147</sup> Just as in the United States, the “fully informed” requirement of the BJR would require directors to ensure that the AI systems they depend on are accurate, transparent and free of bias.<sup>148</sup> Failure to do so would render the decision uninformed, and reliance on such systems without proper oversight could be considered negligence, leading to the loss of BJR protection. By implementing similar policies, South Africa could further develop the role of AI in corporate decision-making, while ensuring that directors remain compliant with their fiduciary duties.

## 5 CONCLUSION

Section 76(5) of the Companies Act permits directors to rely on competent professionals in fulfilling their duties and to delegate certain of their functions. However, since AI systems lack legal personality, directors cannot rely on them directly. Directors can also not delegate their functions to a computer programme such as an AI system. At most, directors can use AI as a research, forecasting and decision-making tool. Directors can use AI to process data and information more efficiently, but they maintain the ultimate decision-making responsibility.

Unlike South Africa, Australia has established reliance principles through the AICD guidelines. These guidelines encourage directors to incorporate AI-based decision-making within their

139 “Blueprint for an AI Bill of Rights” 2022 <https://www.whitehouse.gov/wp-content/uploads/2022/10/Blueprint-for-an-AI-Bill-of-Rights.pdf> (accessed 11-08-2024).

140 Wright “Artificial Intelligence in the States: Emerging Legislation”.

141 Kourinian “A Harmonized AI Governance Framework Starting at the Board & C-Suite Level” 2023 Published by The Bureau of National Affairs Inc <https://www.mayerbrown.com/-/media/files/perspectives-events/publications/2023/04/a-harmonized-ai-governance-framework-starting-at-the-board--csuite-level.pdf?3Frev=9b141e132e6a4f8094d74fb967cf5fa2> (accessed 05-08-2024).

142 *Ibid.*

143 Wright “Artificial Intelligence in the States: Emerging Legislation”.

144 *Ibid.*

145 *Ibid.*

146 South Africa National Artificial Intelligence Policy Framework 2024 <https://www.ellipsis.co.za/wp-content/uploads/2024/04/South-Africa-National-AI-Policy-Framework-August-2024.pdf> (accessed 07-08-2024).

147 Wright “Artificial Intelligence in the States: Emerging Legislation”.

148 See s 76(4)(a)(i) of the Companies Act.

corporate governance frameworks. Australian reliance principles, as provided in AICD guidelines, permit directors to rely on AI systems directly. This removes the need to go through intermediaries like experts. This framework simplifies the process and provides greater clarity on the reliance of directors on AI in decision-making. South Africa should follow suit by establishing its own set of reliance guidelines that specifically address the use of AI systems in decision-making. As a starting point, these policy guidelines should establish at a minimum that when directors do rely on the advice or information provided by an AI system, they should take reasonable steps to ensure that the advice is accurate and reliable, and that they ultimately exercise their own judgement based on the information and advice received. Furthermore, Parliament should formulate an amendment to the Companies Act by incorporating further provisions that clearly define the circumstances in which directors may rely on AI systems and the procedures ensuring the reliability and accuracy of AI-generated information. The amendment should also specify the responsibilities and qualifications of experts who interpret data for directors, therefore ensuring that reliance on AI is done with caution and diligence. The CIPC could then issue further practice notes to clarify the amended legislative principles. However, the key principles and provisions should be integrated into the Companies Act or its regulations to ensure legal clarity and enforceability. This approach would foster a balance between encouraging innovation and ensuring legal accountability. As a result, directors would be provided with the tools to use AI responsibly while maintaining their fiduciary and legal duties outlined under the Companies Act.

Finally, the BJR can be used as a defence by directors when relying on AI, if directors demonstrate that they have taken reasonable steps to be informed, have acted in good faith, and exercised proper diligence even when relying on AI for information and advice. While the use of AI in corporate governance can enhance the quality of business judgments and strengthen directors' ability to invoke the BJR as a defence, reliance on AI can be problematic if directors do not fully understand the complexities of AI algorithms or the potential biases within the data used, leading to uninformed decisions that undermine the protections of the BJR. Given the absence of specific legislation in South Africa governing the matter, it is important to learn from countries such as Australia and the United States that have implemented policy guidelines that assist directors on how to use AI within regulatory bounds.