

**PIERCING THE CORPORATE VEIL IN A HOLDING /
SUBSIDIARY RELATIONSHIP**

by

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CHAPTER 1: INTRODUCTION

1.1 Background of the doctrine of piercing the corporate veil

This research is a review of the extent of powers which the courts have to pierce the corporate veil of a company in a group of companies. The review will be based on the statutory provisions, in particular section 20(9) of the Companies Act 71 of 2008 (the Act)¹, which gives the courts the widest power to pierce the corporate veil. The review will further be based on a discussion of the circumstances providing guidance and justification to disregard juristic personality of a company as a separate juristic entity, as developed in common law.

1.2 Research aims

The research is aimed at determining how the common law position developed to the present position and examining the generally adopted approach to piercing the corporate veil; identifying the circumstances which could possibly justify a finding by a court to pierce the corporate veil; and whether piercing the veil can be used only as a last resort. The paper will further determine if there is a need to develop the specific statutory provisions, so as to enable the courts, to rather preserve the company's legal personality before considering the policies in favour of piercing the veil in a group of companies.

1.3 Research questions

The main question is whether a court can extend the application of the doctrine of piercing the corporate veil to apply to a group of companies as if they are a single entity and thereby piercing the veil of the holding company and ignoring separate legal personalities of the other subsidiary companies in the group. Are the circumstances for piercing the corporate veil as developed in the decision of *Ex Parte Gore*² precise and reassuring to third parties/investors interested in knowing the scope of liability of the shareholders in company activities?

¹ This legislation replaced the Companies Act 61 of 1973 and came into effect on 01 May 2011.

² *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC).

1.4 Methodology and literature review

This research will be based on various sources from South African Law and English Law, but will not be a comparative study. Only one chapter will focus partly on a comparative study of South African Law and foreign legislation and jurisdiction. The recent cases, mainly the judgment in *Ex Parte Gore*, and recent trends will assist in determining whether the law can develop further in view of other legislation, like in insolvency law, and other relevant constitutional values, principles or provisions.³ The development will, in my view, enable the courts to identify other remedies and therefore develop a consistent scope of application of the doctrine of piercing the corporate veil.

Since the main focus is on the doctrine of piercing of the veil in a holding/subsidiary relationship, it will be necessary to also look at the acquisition of shares/shareholding in a company, and definitions of concepts like “control”,⁴ “group of companies”,⁵ “interested person”⁶ and “unconscionable abuse”.⁷ This, in my view, will facilitate the understanding of the scope of liability of controllers, how they escape liability and when they cannot escape liability, for their actions in a company where they have control.

Further, focus will be on the analysis of the elements of “solvency and liquidity”⁸ in a group of companies which must be satisfied when making distribution to shareholders. Here a further aspect of the research will be on whether the assets and liabilities of a company, as a member of a group, should be taken into account together with that of the group, when testing the aforementioned elements.

³ See para 2.1.2 and 6 below.

⁴ See paras 5.1 to 5.2 below.

⁵ See paras 2.2.1 and 5.1 below.

⁶ See para 6.2 below.

⁷ *Ibid.*

⁸ See para 6.3 below.

CHAPTER 2: THE COMPANY CONCEPT AND PRINCIPLE OF SEPARATE LEGAL PERSONALITY

2.1 Company concept

2.1.1 Background and definition of company

A company is a juristic person, separate from its members.⁹ Its property is not the property of its members; its debts are not the debts of its members; and has perpetual succession.¹⁰ From the date and time of registration of its incorporation, a company is considered a juristic person, and exists continually until its name is removed from the companies' register in terms of the Act.¹¹ Its existence is therefore noted formally in a register until its dissolution or deregistration.

Registration as a company bequeaths such an entity with a separate legal personality and as such becomes a legal or juristic entity with rights, obligations and liabilities, like a natural person, although not for all purposes.¹² The purpose of registration is to create legal certainty, and as such, a company becomes eligible to the rights in the Bill of Rights,¹³ to the extent required by the nature of the company and the nature of the rights concerned.¹⁴ Amongst other rights that a company as a juristic person enjoy, is a right to privacy¹⁵ and a right to identity, which the court will protect against unlawful infringement.¹⁶ Therefore, a company has a right to sue for damages in respect of a defamatory statement which is calculated to injure its business reputation.¹⁷

A properly registered company, is relatively a separate entity from its members and therefore a distinct legal *persona*,¹⁸ either individually or as a body.¹⁹ Any activities by

⁹ Pretorius JT *et al South African Company Law through the cases* (1999) 11.

¹⁰ *Ibid.*

¹¹ Section 19(1) of the Companies Act 71 of 2008.

¹² Cilliers HS *et al Cilliers and Benade Corporate Law* (2000) 4. There are activities which a company cannot engage in because it is not human like getting married; see Delpont PA *The New Companies Act Manual* (2011) 10.

¹³ See section 8(2) of the Constitution of the Republic of South Africa, 1996.

¹⁴ Cilliers HS *et al* (2000) 5.

¹⁵ Section 14 of the Constitution of the Republic of South Africa, 1996.

¹⁶ Delpont PA *et al Henochsberg on Companies Act 71 of 2008* (2014) 82. See further *Financial Mail (Pty) Ltd v Sage Holdings Ltd* 1993 (2) SA 451 (A) at 461,463.

¹⁷ Delpont PA *et al* (2014) 82.

¹⁸ Pretorius JT *et al* (1999) 14; see also *Dadoo Ltd v Krugersdorp Municipal Council* 1920 AD 530 at 550.

¹⁹ Delpont PA *et al* (2014) 82.

the company must therefore be distinguishable as those of the company and not of its individual members.²⁰

As a legal person a company has the same capacity and powers as a natural person, except for those things that it cannot do, because it is not a natural person.²¹ It is therefore just as alive and capable of having a will, like human beings. The capacity and powers of a legal person can be restricted further, either by the documents creating the legal person or by the Act that bestows legal personality.²²

In terms of section 19(2) of the Act, a person is not, solely by reason of being an incorporator, shareholder or director of a company, liable for any liabilities or obligations of a company, except to the extent that the Act or the company's Memorandum of Incorporation provides otherwise. This provision resonates with what was stated in the English decision of *Salomon v Salomon*²³ that "the company is at law a different person altogether from the subscribers, being to the memorandum; and though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustee for them".²⁴ Further, the subscribers, as members, are not liable for claims against the company in any shape or form, except to the extent and in the manner provided by the Act.²⁵

Because a company is recognised as a separate legal entity, it is possible for the members of a company to enjoy limited liability. In other words, the doctrine of separate legal personality facilitates limited liability.²⁶ Limited liability means that members of a company are not personally liable for the full extent of their company's debts.²⁷ Also, shareholders are under no obligation to the company or its creditors beyond their obligations on the value of their shares or under the guarantee in the case of a company limited by guarantee.²⁸ Therefore, the extent of the liability depends on the type of

²⁰ Pretorius JT *et al* (1999) 9.

²¹ Delpont PA (2011) 10.

²² *Ibid.*

²³ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

²⁴ *Ibid* at 51. See also Vlasov D *Liability of a puppeteer for a puppet: a recent development in law on piercing the corporate veil* (2012) 11 *The Company Lawyer* 356.

²⁵ *Ibid.*

²⁶ Ciro T *Corporations Law: In Principle* (2013) 66.

²⁷ *Ibid.*

²⁸ Pretorius JT *et al* (1999) 14.

company that has been incorporated. No matter what type of company has been incorporated, if a company has incurred debts, it is primarily liable because its debts are separate from the debts of its members.²⁹ This view is however somewhat altered in section 19(3) of the Act, which provides that directors and past directors of a personal liability company³⁰ will be jointly and severally liable together with the company, for any debts or liabilities of the company contracted during their respective periods of office.

2.1.2 *Acquisition of separate legal personality*

Our legal system recognises acquisition of legal personality in different ways.³¹ Nonetheless, the Act makes provision for two types of companies, namely, profit and non-profit companies.³² Acquisition of legal personality can be by general enabling Act, specific Act or conduct.

A general enabling Act gives legal personality to all entities, and not to a specific entity, as long as, the entities comply with the requirements of that Act.³³ In our legal system, the most important type of a general enabling Act is the Act (Companies Act 71 of 2008).³⁴ The Act obviously applies in respect of a company as defined in its section 1.³⁵

Some Acts expressly provide that the entity formed in terms of their provisions has legal personality.³⁶ For example, the Scientific Research Council Act No. 46 of 1988 provides in section 2(1) that the Council for Scientific and Industrial Research is a juristic person.³⁷ Although the Council for Scientific and Industrial Research is a juristic person, the Act does not apply, because the juristic personality was not acquired in terms of the Act.³⁸ In respect of some companies, both the Act and their enabling Acts apply, like the South

²⁹ Ciro T (2013) 66.

³⁰ Section 8(2) of the Act.

³¹ Cilliers HS *et al* (2000) 6.

³² Delpont PA *et al* (2014) 48(1).

³³ Delpont PA (2011) 10.

³⁴ *Ibid.*

³⁵ Section 1 provides that a company is a juristic person incorporated in terms of this Act, a domesticated company, or a juristic person that, immediately before the effective date was registered in terms of the Companies Act, 1973 (Act No. 61 of 1973), other than as an external company as defined in that Act; or Close Corporations Act, 1984 (Act No. 69 of 1984), if it has subsequently been converted in terms of Schedule 2 was in existence and recognised as an "existing company" in terms of the Companies Act, 1973 (Act No. 61 of 1973); or was deregistered in terms of the Companies Act, 1973 (Act No. 61 of 1973), and has subsequently been reregistered in terms of this Act.

³⁶ Delpont PA (2011) 10.

³⁷ Delpont PA *et al* (2014) 48(1).

³⁸ *Ibid.*

African Post Office SOC Limited³⁹ or the Land and Agricultural Development Bank of South Africa.⁴⁰

Where a group of people conducts themselves like a legal or juristic person, the common law recognises such an association of persons as a legal person and thus obtain legal personality as a result of their conduct.⁴¹ The characteristics of such an association are that it should be capable of owning property, apart from its members and it should have perpetual succession.⁴² In *Webb & Co v Northern Rifles*,⁴³ it was held that amongst the most important rights appertaining to an *universitas* is the right to acquire and hold property.

An association of persons formed after 31 December 1939, for purposes of carrying on any business that has for its object the acquisition of gain by the association or its members, is or may be a company or other form of body corporate, if it is registered as a company under the Act, is formed pursuant to another law, or was formed pursuant to Letters Patent or Royal Charter before 31 May 1962.⁴⁴

The object of gain does not have to be pecuniary, as long as, there's commercial or material benefit or advantage.⁴⁵ If the membership of an association exceeds 20, the association must be registered as a company, if it is formed for the critical purpose, failing which it will have no *locus standi*.⁴⁶ In *Morrison v Standard Building Society*,⁴⁷ decided before 31 December 1939 it was held that in order to determine whether an association of individuals is a corporate body, which may sue or be sued in its own name, the court has to consider the nature and objects of the association, as well as, its constitution, and if these show that it possesses the characteristics of a corporation or *universitas* then it can sue in its own name.⁴⁸

³⁹ In terms of the South African Post Office SOC Limited Act 22 of 2011.

⁴⁰ In terms of the Land and Agricultural Development Bank Act 15 of 2002.

⁴¹ Delpont PA (2011) 10.

⁴² Delpont PA *et al* (2014) 48(1).

⁴³ *Webb & Co v Northern Rifles* (1908) TS 462.

⁴⁴ Delpont PA (2011) 10. See further section 8(3) Companies Act 71 of 2008 and section 31 of the *Companies Act* 68 of 1973.

⁴⁵ *Mitchell's Plain Town Centre Merchants Association v Mcleod* 1996 (4) SA 159 (SCA) at 169-170.

⁴⁶ *Ibid* at 167.

⁴⁷ *Morrison v Standard Building Society* (1932) AD 229.

⁴⁸ *Ibid* at 237.

2.1.3 Case analysis

The main decision in support of the principle of separate legal personality was in the matter which came before the House of Lords in *Salomon v Salomon*⁴⁹. The facts in this matter were briefly as follows. Mr Salomon sold his business to a duly registered company in which he was a managing director and shareholder amongst 7 shareholders. He subscribed to the majority of the shares in the company and the other 6 shareholders who were his family members subscribed to 1 share each of the 6 remaining shares. The company was later liquidated and subsequent to payment of secured creditors and Mr Salomon's debentures, nothing remained for unsecured creditors. The liquidator alleged that the incorporation of the company was fraud and used to avoid liability by Mr Salomon, for debts of the company in particular claims by unsecured creditors. In the High Court, Judge Vaughan Williams ruled that Mr Salomon, was the principal and the company his agent, and therefore liable for the debts of unsecured creditors. The liquidator succeeded in the Court of Appeal where the judge confirmed the High Court ruling on different grounds that Mr Salomon abused the privileges of incorporation and limited liability for his own benefit, enabling him to incur debts in the company name and avoid liability. However, the House of Lords reversed the decision of the court *a quo* and Lord Halsbury LC held that "it seems to me impossible to dispute that once the company is legally incorporated it must be treated like any other independent person its rights and liabilities appropriate to itself, and that the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are".⁵⁰

In *Dadoo Ltd v Krugersdorp Municipality Council*⁵¹ Innes CJ held that this conception of the existence of a company as a separate entity distinct from its shareholders is not merely artificial and technical thing. It is a matter of substance; property vested in the company is not, and cannot be, regarded as vested in all or any of its members.

It is clear from the decisions in *Salomon v Salomon*⁵² and *Dadoo v Krugersdorp Municipality Council*,⁵³ as well as in cases which followed thereafter that a company once registered in terms of the laws governing incorporation, it stands out as an entity separate

⁴⁹ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL). See also Pretorius JT *et al* (1999) 12 for a discussion of *Salomon v Salomon* under this subject.

⁵⁰ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 30.

⁵¹ *Dadoo Ltd v Krugersdorp Municipality Council* 1920 AD 530, at 550-551.

⁵² *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

⁵³ *Dadoo Ltd v Krugersdorp Municipality Council* 1920 AD 530.

from its members or shareholders, even though, the business remains as is after incorporation⁵⁴ and that the property of the company cannot be vested in its members.

2.2 Separate legal personalities of companies in a group

2.2.1 *Background and definition of group of companies*

A group of companies comprises a holding company and all its subsidiaries.⁵⁵ A holding company in relation to a subsidiary is a juristic person that controls that subsidiary company if it is able to directly or indirectly exercise or control the exercise of majority voting rights associated with securities of that subsidiary company; or has the right to appoint or elect, or control the appointment or election of directors of that subsidiary company, who control the majority of the votes at a meeting of the board of directors.⁵⁶

In *Unisec Group Ltd v Sage Holdings Ltd*,⁵⁷ the directors of Unisec decided that two companies, that is Newstock and Billhawk, which are wholly owned subsidiaries, should purchase Unisec shares. The issue here was whether Unisec controls, within the meaning of holding company in the old Companies Act⁵⁸, the composition of the board of directors in Newstock. This raised the question, whether Unisec's exercise of its rights to acquire shares in its subsidiary, is the exercise of some power whereby it may appoint the majority of directors. It was held that from the moment that Unisec acquired rights to obtain the shares, Newstock became a subsidiary of Unisec.

Where a holding company is linked with a subsidiary or subsidiaries to form a larger and more complex economic units, these companies are usually referred to as a group.⁵⁹ The basic characteristic of such a group is that the management of the different independent holding and subsidiary companies comprising a group, is co-ordinated in such a way that it takes place on a central and unified basis in the interests of the group as a whole.⁶⁰ This management on a unified basis is possible because of the control, implicit in the

⁵⁴ Pretorius JT *et al* (1999) 13. See also *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 50.

⁵⁵ Section 1 of the *Companies Act* 71 of 2008. See also Delpont PA (2011) 105.

⁵⁶ Sections 1, 2(2)(a) and 3(1)(a) of the *Companies Act* 71 of 2008.

⁵⁷ *Unisec Group Ltd v Sage Holdings Ltd* [1986] 3 SA 259 (T).

⁵⁸ Act 61 of 1973.

⁵⁹ Cilliers *et al* *Cilliers and Benade Corporate Law* (1999) 432. See also Botha DH *Groups in South African Company Law* (1981) LLD Thesis UP 63.

⁶⁰ *Ibid.*

holding/subsidiary relationship, which the holding company exercises over the subsidiary or subsidiaries.⁶¹

2.2.2 *Legal position in holding/subsidiary relationship*

As alluded to above, the definition of holding company and subsidiary relationship focuses on control.⁶² The power to control is the determining factor as to whether one company is a subsidiary to another.⁶³ The purpose for the definition of holding/subsidiary company relationship was originally to form the basis for disclosure of the financial position of a company and its subsidiary(ies) by way of group financial statements and also utilized in the past to prevent abuse of its control by a holding company over its subsidiary.⁶⁴

This control makes it possible for the group to be managed as an economic unit, in the sense that the different holding and subsidiary companies no longer carry out their commercial activities on a footing of complete economic independence.⁶⁵ Auditors also have a duty to ensure that, where the holding/subsidiary company group relationship exists, they give effect to the disclosure and abuse of control provisions.⁶⁶

Although, South African courts have often referred to a group, they have never regarded a holding company and its subsidiary(ies) as constituting a separate independent *persona*, apart from the *personae* of the independent constituent companies, comprising a group.⁶⁷ The South African and English courts have on the contrary, influenced by the decision in Salomon's case, emphasised the separate legal personality and interests of the different holding companies and subsidiaries.⁶⁸

As indicated above, a company is a subsidiary of another juristic person if that juristic person, one or more other subsidiaries of that juristic person, or one or more nominees of that juristic person or any of its subsidiaries, alone or in any combinations, is or are directly able to exercise, or control the exercise of a majority of the general voting rights

⁶¹ Cilliers HS *et al* (1999) 432.

⁶² *Ibid* at 433.

⁶³ Delport PA *et al* (2014) 29.

⁶⁴ Botha DH (1981) 11.

⁶⁵ Cilliers HS *et al* (1999) 432. See also Botha DH (1981) 63.

⁶⁶ Botha DH (1981) 61.

⁶⁷ *R v Milner & Erleigh* 1951 (1) SA 791 (A) 810-812. See also Botha DH (1981) 68-69.

⁶⁸ Botha DH (1981) 69.

associated with issued securities of that company, whether pursuant to a shareholder agreement or otherwise; or has or have the right to appoint or elect, or control the appointment or election of, directors of that company who control a majority of the votes at a meeting of the board; or a wholly-owned subsidiary of another juristic person if all of the voting rights⁶⁹ associated with issued securities of the company are held or controlled, alone or in any combination, by persons contemplated in section 3(1)(a) of the Act.⁷⁰

The determinants for holding/subsidiary relationships apply in respect of the juristic person alone, or in any combination with any of its subsidiaries or nominees.⁷¹ It would therefore also be a holding/subsidiary relationship if the juristic person has the sole control of the majority of the voting rights in a company, whether pursuant to an agreement with other members of the said company or otherwise; or the company is a subsidiary of a juristic person which is a subsidiary of the juristic person; or subsidiaries of the juristic person, or juristic person and its subsidiaries together, (a) hold the majority of the voting rights in the company or (b) have the right to appoint the directors holding a majority of the voting rights at meetings of the board of directors of the company or (c) have the sole control of the majority of the general voting rights in the company whether pursuant to an agreement with other members of the company or otherwise.⁷²

In terms of the *Salomon v Salomon* judgment,⁷³ in the absence of fraud, the holding company, as incorporator or otherwise of the subsidiary, is distinct or separate from the company as legal person possessing its own interests, rights, assets and liabilities. By the same token the subsidiary will also be a separate legal *persona* possessing its own interests, rights, assets and liabilities. It is further stated in the judgment that the fact that the holding company is able to control the subsidiary or hold all of the shares in it does not make the subsidiary its agent.

On the strength of the *Salomon v Salomon* judgment, a subsidiary is therefore not regarded as the agent of its holding company merely as a result of this relationship.⁷⁴ Although the basis of the holding/subsidiary company relationship is control, this fact

⁶⁹ These are voting rights as determined by the Memorandum of Incorporation of a company. See Delpont PA *et al* (2014) 30(5).

⁷⁰ See section 3(1)(a) of the *Companies Act* 71 of 2008. See also Delpont PA *et al* (2014) 35(2).

⁷¹ Delpont PA *et al* (2014) 35(2).

⁷² *Ibid.*

⁷³ See Cilliers HS *et al* (2000) 432 for a discussion of the *Salomon* judgment. See also Botha DH (1981) 65.

⁷⁴ Botha DH (1981) 83.

alone will not make the subsidiary agent of its holding company, even if, it is wholly owned.⁷⁵ As a consequence of the separate personalities of the holding and subsidiary companies, the subsidiary itself, and not its holding company, will have to institute action and enforce its rights.⁷⁶ Similarly, a subsidiary cannot either institute action to enforce the rights of its holding company.

On another hand, the provisions governing the submission of group financial statements are based on the concept that the larger economic unit of companies constitutes a group forming a single accounting entity; the holding company and subsidiaries do not thereby lose their separate legal personalities.⁷⁷ This position was investigated in *Ex Parte Gore* where it was found that the group conducted its businesses in a manner that would make it difficult to identify each company in the group, and in effect the systems and functions of the whole group were controlled and ran as one through the parent company.⁷⁸

Whether or not the holding company benefits from limited liability as against the subsidiary, the shareholders of the holding company cannot lose more than the value of their investments provided the holding company is subject to the doctrine [of limited liability].⁷⁹ Because of the unified control exercised throughout a group, the Act and the courts, especially in the United Kingdom, appear to consider that for certain purposes the importance of the academic unit of the group as a whole overrides that of the different economically independent holding and subsidiary companies.⁸⁰

2.2.3 *Duties of directors in a holding/subsidiary relationship*

The fiduciary duties of directors serve to protect the company, and consequently its shareholders and creditors against its directors misapplying its assets. However, the director may be placed in an impossible position, where there is a potential conflict between his fiduciary duty to the subsidiary and his interest due to the fact that he is subject to instructions from the holding company's directors, who through the holding company can control him.⁸¹

⁷⁵ *Ibid.*

⁷⁶ Botha DH (1981) 66. See also *Foss v Harbottle* 1843 ER 189.

⁷⁷ Cilliers HS *et al* (1999) 432-433.

⁷⁸ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 442.

⁷⁹ Davies PL *Gower Principles of Modern Company Law* (2016) 193.

⁸⁰ Botha DH (1981) 3.

⁸¹ Botha DH (1981) 222 at 249.

The traditional common law view is thus that holding and subsidiary companies possess their own legal personalities, rights, assets and liabilities.⁸² This traditional common law approach has however, become subjected to pressures in order to give effect to the realities of control that exist in groups.⁸³

Legal problems could, however, arise in cases where this personality existed simultaneously with the personality of the different companies regarding the position of amongst others, directors, creditors and shareholders of the different holding and subsidiary companies.⁸⁴ Will the directors owe their duties to the all-embracing personality, as well as, to the company to which they are officially appointed?⁸⁵ Are the creditors, creditors of the group assets, as well as, creditors of the different companies?⁸⁶ These questions will be dealt with in detail below.⁸⁷

2.3 The effect of legal personality

2.3.1 *Background*

Once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are.⁸⁸ The company is therefore a separate legal subject, independent of its constituent shareholder/s,⁸⁹ and thus legal consequences flow from such separate legal personality.⁹⁰ Upon incorporation, a natural person, who is a sole shareholder, actually creates a second legal subject, the legal or juristic person, apart from him, the natural person.⁹¹

2.3.2 *Consequences of legal personality*

The fact that a company upon registration has separate legal personality embodies it with separate legal existence; perpetual existence in the sense that a change in members

⁸² Cilliers HS *et al* (1999) 432. See also Botha DH (1981) 67.

⁸³ Cilliers HS *et al* (1999) 432.

⁸⁴ Botha DH (1981) 89.

⁸⁵ *Ibid.*

⁸⁶ Botha DH (1981) 89.

⁸⁷ The details are discussed in chapters 5 and 6 below.

⁸⁸ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 30. See also Delport PA (2011) 11, and para 2.1.3 *supra*.

⁸⁹ Delport PA (2011) 11.

⁹⁰ Cassim FHI *et al Contemporary Company Law* (2012) 35.

⁹¹ Delport PA (2011) 11.

does not affect the legal person; the entity becomes a legal subject and has all the rights of a legal subject, including, amongst others, suing and being sued in its own name; the entity cannot act in its own name; and the entity is bound by and entitled to the Bill of Rights in terms of section 8(2) of the Constitution of the Republic of South Africa, 1996.⁹² This creates a basis for limited liability for members of the company.

2.4 Conclusion

Juristic personality is a legal fiction which in essence is a figment of law,⁹³ and thus, in the event that there is improper use of the juristic personality, courts will disregard it, if it is found that the use is inconsistent with the purpose for which it was created.⁹⁴ This is essentially the application of the doctrine of piercing the corporate veil.

⁹² *Ibid.*

⁹³ *Ebrahim v Airports Cold Storage (Pty) Ltd* 2008 (6) SA 585 (SCA) at 592.

⁹⁴ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 441.

CHAPTER 3: THE DOCTRINE OF PIERCING THE CORPORATE VEIL (IN GENERAL)

3.1 Introduction and background

When a company is registered and thereby acquires legal personality, a hypothetical blanket or shroud drops over its shareholders and directors for protection from external accountability.⁹⁵ This consequently separates the new company from the people who formed it, and from those who go on to become its members and directors.⁹⁶ It is trite law that, a registered company is a legal *persona* distinct from the members who compose it.⁹⁷ A company's separate legal existence is therefore referred to as a veil of incorporation, for as long as, there is no external interference.⁹⁸

Legal personality is not a doctrine without challenges, it can be ignored by piercing the corporate veil,⁹⁹ and thus liability of the company could be found to be liability of its members. It is significant to consider that once the company acquires a separate legal existence through incorporation the veil allows the company directors to operate the company without external interference, unless they use the company for illegal purposes.¹⁰⁰

As an entity, a company consists of component parts like directors and shareholders.¹⁰¹ It is as such an aggregate of component parts, on the one hand, and an entity which, as a whole, differs from the mere aggregate of its components.¹⁰² Company law philosophy allows the company to be viewed as a separate entity or from a point of view of its separate component parts.¹⁰³ The *Salomon* case established that, provided the legislative formalities are complied with, a company will be validly incorporated, even if it's a "one person" company, and the courts will be reluctant to treat a shareholder as personally liable for the debts or liabilities of the company by "piercing the corporate veil".¹⁰⁴ On the other hand, a court would be justified in certain circumstances in

⁹⁵ Cassim FHI *et al* (2012) 41. See also Fitzpatrick JF *et al* *Business and Corporations Law* (2014) 425.

⁹⁶ *Ibid.*

⁹⁷ Pretorius JT *et al* (1999) 31. See also *Dadoo Ltd v Krugersdorp Municipal Council* 1920 AD 530 at 550 and *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 817.

⁹⁸ Fitzpatrick JF *et al* (2014) 425.

⁹⁹ Delpont PA (2011) 12.

¹⁰⁰ Fitzpatrick JF *et al* (2014) 425.

¹⁰¹ Cilliers HS *et al* (2000) 11.

¹⁰² *Ibid.*

¹⁰³ Cilliers HS *et al* (2000) 11.

¹⁰⁴ Davies PL (2016) 202.

disregarding a company's separate personality in order to fix liability elsewhere for what are ostensibly acts of the company.¹⁰⁵ This is generally referred to as piercing or lifting the corporate veil.¹⁰⁶

Piercing the corporate veil is a phrase used to consider the rights or activities of an entity as those of its members or shareholders.¹⁰⁷ Piercing or lifting the corporate veil is a legal concept or phrase used when taking into consideration the shareholding of the controllers or members of a company in determining legal disputes or for some legal purpose.¹⁰⁸ It is also a phrase somewhat extensively used to describe a number of different things, and properly speaking, it means disregarding the separate personality of the company.¹⁰⁹ It is widely accepted that if a company is incorporated for no proper purpose, but as frontage in concealment of true facts, separate personality of a company will be disregarded.¹¹⁰ This may be in terms of either the common law or specific statutory provisions, as discussed below.

3.2 When is legal personality ignored in terms of common law?

The courts are prepared in certain instances to peer through the corporate veil in order to give effect to the reality behind the façade of a company or even to ignore separate existence of the legal person or to lift or pierce the corporate veil.¹¹¹ Further, policy consideration and fairness may require that corporate entity be ignored, and the circumstances will thus depend on the facts of each case.¹¹² Therefore, courts will ignore the principle of separate legal personality if it could be determined that the company is used improperly and contrary to the purpose of the existence of a company as a legal person.¹¹³ In effect, when the courts pierce the corporate veil, they remove the protection of limited liability otherwise granted to shareholders.¹¹⁴

¹⁰⁵ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) 790 (A) at 802. See also Pretorius JT *et al* (1999) 31.

¹⁰⁶ *Ibid.*

¹⁰⁷ *Atlas Maritime Co SA v Avalon Maritime Ltd (The Coral Rose) (No.1)* [1991] 4 All ER 769 (CA) at 779. See also *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 440.

¹⁰⁸ *Ibid.*

¹⁰⁹ *Prest v Petrodel Resources Ltd* [2013] UKSC 34 at para 16.

¹¹⁰ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 450.

¹¹¹ Cilliers HS *et al* (2000) 13.

¹¹² Delpont PA (2011) 12.

¹¹³ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 441.

¹¹⁴ Ramsay IM *Piercing the corporate veil in Australia* (2001) 19 Companies and Securities LJ 250.

The grounds on which the courts will pierce the corporate veil are said to have been difficult to state with certainty.¹¹⁵ For example, courts cannot ignore corporate personality by piercing the corporate veil only on the basis that it is in the interest of justice.¹¹⁶ It is not a general discretion and therefore should be based on circumstances which may lead to and justify piercing the corporate veil.¹¹⁷ These grounds for piercing the corporate veil are derived from application of the common law by the courts. Common law principles for the doctrine of piercing the corporate veil in a group of companies are discussed in chapter 4 below.

3.3 When is legal personality ignored in terms of statutory law?

Apart from the common law, the general principle of piercing the corporate veil is now codified in the Act.¹¹⁸ Section 20(9) of the Act¹¹⁹ affords courts a statutory legal foundation and source for piercing or lifting the corporate veil of companies.¹²⁰ This provision affords aggrieved parties, like investors and creditors, protection and thereby protection of the assets of the company,¹²¹ in terms of approaching the court for piercing of the corporate veil.¹²²

Section 20(9) is not an ultimate remedy, it can be used at any time even where there are other remedies and where the basis for the claim is not clear. There are other provisions of the Act in terms of which the separate legal personality of the company may be ignored. For example, section 22 provides that a company's business may not be conducted recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose, otherwise it may be ordered to cease trading or conducting business by the Commission¹²³ or its directors may be held liable to the company for any damage, loss or costs arising from the prohibited conduct.¹²⁴ Further, any creditor affected by the

¹¹⁵ Cassim FHI *et al* (2012) 42.

¹¹⁶ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) 790 (A) at 803.

¹¹⁷ *Ibid.*

¹¹⁸ Delpont PA *et al* (2014) 100(3).

¹¹⁹ Section 20(9) of the *Companies Act* 71 of 2008.

¹²⁰ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 451.

¹²¹ Cassim R *Hiding behind the veil* (2013) 535 De Rebus 35.

¹²² *Ibid.*

¹²³ The Companies and Intellectual Property Commission can in this regard issue a compliance notice to a company trading fraudulently. See further Delpont PA *et al* (2014) 104.

¹²⁴ Delpont PA *et al* (2014) 105.

prohibited trading may institute a claim for damages in terms of section 218(2) against the directors.¹²⁵

Section 20(9) of the Act provides a similar remedy to that in section 65 of the Close Corporations Act 69 of 1984, in respect of close corporations. On the other hand, section 22 of the Act is comparable to the sections 424, 425 and 426 of the old Companies Act 61 of 1973, respectively. Therefore, when interpreting or applying the provisions of section 20(9) of the Act, guidance could be had or gained from the other legislative provisions referred to above.

3.4 Case analysis

In *Botha v Van Niekerk*,¹²⁶ the court was asked to lift the veil in order to enforce a sale contract against Van Niekerk, the sole director of a duly incorporated company. It was held that if there was an unconscionable injustice in the sense that a court in general cannot countenance, then the separate legal personality can be ignored. The application was dismissed as there was no unconscionable injustice. The test here is objective.

In *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*,¹²⁷ it was held in the minority judgment that piercing of the corporate veil should not necessarily be precluded if another remedy exists.¹²⁸ It was held in the Appeal Court that if there's fraud, dishonesty and improper conduct, legal entity can be disregarded. Improper conduct is not fraud or dishonesty, as there is no element of intent or gross negligence or recklessness. It was stated that it is not necessary that a company should have been conceived and founded on deceit, and never have been intended to function genuinely as a company before its corporate personality may be disregarded. Therefore, it does not matter whether the company was initially created for the sole reason of evading legal obligations arising from a specific agreement or was for a legitimate cause from inception and only later used improperly, its separate legal personality may in any way be disregarded.¹²⁹ The subjective motives are therefore irrelevant.

¹²⁵ *Ibid.* See further section 218(2) states that "Any person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention."

¹²⁶ *Botha v Van Niekerk* 1983 (3) SA 513.

¹²⁷ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A). See also Delpont PA (2011)12.

¹²⁸ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* at 805.

¹²⁹ Cassim FHI *et al* (2012) 45.

In *Consolidated News Agencies (Pty) Ltd (in liquidation) v Mobile Telephone Networks (Pty) Ltd*¹³⁰ it was stated that the actions of the directing mind and will of the company will be that of the company for criminal and delictual liability, as well as, for determining the intention of the company for income tax purposes.

In *Manong & Associates v City of Cape Town*¹³¹ the issue was, amongst others, whether a juristic person can be a victim of racial discrimination. The court held that the complainant is a disadvantaged juristic person, like natural persons, with rights worthy of protection by the constitution, and found that the complainant is a victim of racial discrimination.

However, there has to be some unfair advantage or result derived from the abuse of separate personality. In *Hülse Reutter and Others v Gödde*¹³² it was held that there must at least be some misuse or abuse of the distinction between the corporate entity and those who control it, which results in an unfair advantage being afforded to the latter.

In *VTB Capital plc v Nutritek International*,¹³³ the issue to be determined also in the Supreme Court (of the United Kingdom) was whether, in a case where a person uses a puppet company to enter a contract with a third party in order to perpetrate fraud on that third party, a court can pierce the corporate veil and treat that person as a party to the contract. In the Court of Appeal, Munby J stated that, it was not necessary in order to pierce the corporate veil that there should be no other remedy available against the wrongdoer.¹³⁴ It was further stated that it was not enough to show that there had been wrongdoing to justify piercing. However, where wrongdoing exists, the relevant wrongdoing must be in the nature of an independent wrong that involves the fraudulent or dishonest misuse of the corporate personality of the company for the purpose of concealing the true facts. The perception that there is no principled basis upon which it can be said that one can pierce the veil of incorporation receives some support from the fact that the precise nature, basis and meaning of the principle are all somewhat obscure, as are the precise nature of circumstances in which the principle can apply. Lord

¹³⁰ *Consolidated News Agencies (Pty) Ltd (in liquidation) v Mobile Telephone Networks (Pty) Ltd* 2010 (2) All SA 9 (SCA). See also Delpport PA (2011) 12.

¹³¹ *Manong & Associates v City of Cape Town* 2009 (1) SA 644 (EqC). See also Delpport PA (2011) 12.

¹³² *Hülse-Reutter and Others v Gödde* 2001 (4) SA 1336 (SCA).

¹³³ *VTB Capital plc v Nutritek International* [2013] UKSC 5.

¹³⁴ See Delpport PA (2011) 12.

Neuberger suggested that generally it may be right for the law to permit the veil to be pierced in certain circumstances in order to defeat injustice. Lord Neuberger noted that even if the court could in principle pierce the corporate veil, doing so in the claimed circumstances would be close to extending the concept in a manner contrary to principles. There are two principles which Lord Neuberger was of the view they will be in contrast with the extension of the concept. The first one is the lack of need or exceptional ground to depart from the principle of disregarding the corporate personality of the alleged puppet company, due to the fact that the law of delict already provided VTB with a remedy for negligent or fraudulent misrepresentation. The second principle, was that VTB wanted to introduce allegations into its founding pleading which would not have established that the puppet company was used as frontage in concealment of the true facts.¹³⁵

In *Adams v Cape Industries*¹³⁶ the issue was whether the United Kingdom parent of an international mining group which was seemingly managed as a “single economic unit” was present in the United States for the purpose of making a default judgment of a United States court enforceable against it in England. The court held that the corporate veil could be disregarded only in cases where it was being used for a deliberately dishonest purpose. It was stated that, as a matter of law, the corporate veil can be lifted in appropriate circumstances. The court further held that the court is not free to disregard the principle of separate legal personality merely because it just to do so.¹³⁷

Although, the courts are prepared to disregard a company’s separate legal personality in certain cases, Smalberger JA remarked, in *Cape Pacific v Lubner Controlling Investments*¹³⁸ that courts should not lightly disregard a company’s separate corporate personality, but should try to give effect to it. It was held further that to do otherwise would be to negate or undermine the policy and principles that underpin the concept of separate corporate personality and the legal consequences that attach to it.¹³⁹ But, where fraud, dishonesty or other improper conduct is found to be present, other consideration will come into play.¹⁴⁰ The need to preserve the separate corporate identity would in such circumstances have to be balanced against public policy considerations which arise in

¹³⁵ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 448.

¹³⁶ *Adams v Cape Industries plc* [1991] 1 All ER 929 (CA).

¹³⁷ [1991] 1 All ER 929. See also *Prest v Petrodel Resources Limited* UKSC 34 at para 21.

¹³⁸ *Cape Pacific v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A). See also Cilliers et al *Cilliers & Benade Corporate Law* (2000) 15.

¹³⁹ Cilliers HS et al (2000) 15.

¹⁴⁰ *Ibid.*

favour of piercing the corporate veil.¹⁴¹ Smalberger JA held further that, it is probably fair to say that a court has no general discretion simply to disregard a company's separate legal personality, whenever it considers it just to do so. The Honourable Judge also observed that the law is far from settled with regard to the circumstances in which it would be permissible to pierce the corporate veil.¹⁴²

The above discussion and other South African authorities show that courts will disregard the corporate personality of a company irrespective of the repeated pronouncement that there is no general discretion afforded courts to do so merely because it is just and equitable, but when dictates of justice so demand.¹⁴³ Therefore, courts will disregard the corporate personality not only when there is no other remedy available, but based on the requirements of justice, and, in most cases, fraud or improper conduct is present where the corporate veil is pierced or lifted.¹⁴⁴

The circumstances in which an English court will be prepared to pierce the corporate veil as set out in *Ben Hashem v Ali Shayif*¹⁴⁵ perhaps reflects the correct position currently in that jurisdiction, other than the proposition that the court will pierce the corporate veil of a company for the sole purpose and extent of providing a remedy against the controllers of the company in respect of a particular wrong committed by the controllers.¹⁴⁶ In this case, Munby J set out the following principles:¹⁴⁷ 1. ownership and control of a company do not on their own justify piercing the corporate veil; 2. the court cannot pierce the veil simply because it is perceived that to do so is necessary in the interest of justice; 3. the corporate veil can only be pierced when there is some impropriety in the company; 4. the impropriety must lead to the use of the company structure to avoid or conceal liability; 5. both control of the company by the wrongdoer and impropriety in the sense of a misuse of the company as a device or façade to conceal wrongdoing must be for the benefit of the person who control the company; a company can be a façade for such purposes even though it was not incorporated with intention to deceive and the relevant question will be whether the veil can be pierced for a particular transaction(s) at any time during the life of the company; and 6. the court will pierce the veil only so far as is necessary to provide

¹⁴¹ Cilliers HS *et al* (2000) 15.

¹⁴² *Cape Pacific v Lubner Controlling Investments* 1995 (4) SA 790 (A) at 802.

¹⁴³ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 450.

¹⁴⁴ *Ibid.*

¹⁴⁵ *Ben Hashem v Ali Shayif and Another* [2008] EWHC 2380 (Fam).

¹⁴⁶ *Ibid.* See also *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 446.

¹⁴⁷ *Ben Hashem v Ali Shayif and Another* [2008] EWHC 2380 (Fam) at paras 159-164.

a remedy for the particular wrong which those controlling the company have done. Consequently, the fact that a court pierces the veil for one purpose does not mean that it will necessarily be pierced for all purposes.

In *Prest v Petrodel*¹⁴⁸ a recent case on the doctrine, a wife lodged an application in the Supreme Court of the United Kingdom following a number of applications, the last being in the Court of Appeal against a group of companies, claiming transfer of properties owned by some of the companies in the group, allegedly for the benefit of her husband. There was no issue about the matrimonial home which was being transferred to the wife. These companies were found by the judge in the court *a quo* to be wholly owned and controlled by the husband. The issue to be decided in the Court of Appeal was whether the court has the power to order transfer of these seven properties to the wife given that they legally belong to the husband's companies and not to him. The distinctive feature of the judge's approach was that he concluded that there was no general principle of law which entitled him to reach the companies' assets by piercing the corporate veil. This was because the authorities showed that the separate legal personality of the company could not be disregarded, unless it was being abused for a purpose that was, in some relevant respect, improper. The judge held that there was no relevant impropriety. However, the wife succeeded on the basis that the properties were held for the benefit of the husband, but her claims dismissed in so far as it relies on the piercing of the corporate veil. This decision deviates from decision of the Court of Appeal in *VTB Capital*¹⁴⁹ case.

3.5 Conclusion

The circumstances in which it would be permissible to pierce the corporate veil seem far from settled with regard to the separate legal personality of a company and those who control it. Enquiring into and determining the facts of each case, policy consideration and case law, may be of great significance.¹⁵⁰

It appears however to have been recognised that proof of fraud or dishonesty might justify disregarding the separate corporate personality.¹⁵¹ Over the years it has come to be accepted that fraud, dishonesty or improper conduct could provide grounds for piercing

¹⁴⁸ *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

¹⁴⁹ *VTB Capital plc v Nutritek International Corp* [2012] EWCA Civ 808.

¹⁵⁰ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A).

¹⁵¹ *Ibid* at 803.

the corporate veil.¹⁵² Some authorities hold that piercing the corporate veil so as to make the controllers of a company jointly and severally liable on the company's contract creates a new liability that would not otherwise exist.¹⁵³ The Lord of Justices of the Supreme Court in *VTB Capital* case were unanimous in their decision that the pivotal principle of company law set by the *Salomon* case should be upheld, and that the law does not allow treating a person, although being in control of a company, as being liable in breach of an agreement concluded by the company.¹⁵⁴

The independence of the entity is thus not always viewed realistically and therefore emphasis is often placed on the sacredness of the entity, instead of regarding it as a feature of the whole.¹⁵⁵ Nevertheless a situation involving the company and its members or representatives is judged with due consideration to the actual state of affairs pertaining within the company behind the corporate entity.¹⁵⁶

Generally, in deciding whether to pierce or lift the veil in statutory cases, the courts are guided by their understanding of the statute in question, and so, the decision to be made is likely to differ from statute to statute.¹⁵⁷ The legislature developed rules to impose liability on shareholders or directors of companies in the case of abuse of limited liability.¹⁵⁸

¹⁵² *Ibid.*

¹⁵³ *VTB Capital plc v Nutritek International Corp* [2013] UKSC 5. See also *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

¹⁵⁴ Vlasov (2013) 34 *The Company Lawyer* 248 at 252.

¹⁵⁵ Cilliers JT *et al Cilliers & Benade Corporate Law* (2000) 11.

¹⁵⁶ *Ibid.*

¹⁵⁷ Davies PL (2016) 199.

¹⁵⁸ *Ibid* 206.

CHAPTER 4: APPROACHES TO PIERCING THE CORPORATE VEIL IN A GROUP OF COMPANIES

4.1 Introduction and background

Companies in a group are perceived as separate legal entities. However, the courts have in the commercial framework, dealt with a group as an economic entity.¹⁵⁹ Piercing of the corporate veil is applicable particularly when a holding company owns all the shares of the subsidiaries, to an extent that, it can control the entire governance of the subsidiaries.¹⁶⁰

Business deals between a subsidiary and its holding company are not similar to those of independent and unrelated parties, who require the best outcome of their deal. The distinct element of the holding/subsidiary relationship is that the holding company exercises some defined control over the subsidiary.¹⁶¹

The effect of the principles in the United Kingdom's decision in *Adams v Cape Industries*¹⁶² is that the law recognises the creation of companies, which though in one sense are creatures of their incorporating parent entities or incorporators will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities.¹⁶³ This principle, to some extent, influenced South African legal system.

The courts have however been divided in their approach or application of the doctrine of piercing the corporate veil in the group context. This is more so as to whether and in what circumstances the corporate veil of the group may be pierced, so that the group is in fact viewed as a single entity, as opposed to, a collection of different corporate entities.¹⁶⁴

¹⁵⁹ Cilliers HS *et al* (2000) 437. See also *DHN Food Distributors Ltd v London Borough of Tower Hamlets* [1976] 1 WLR 852.

¹⁶⁰ *Ibid.*

¹⁶¹ Cilliers HS *et al* (2000) 443.

¹⁶² *Adams v Cape Industries plc* [1991] 1 All ER 929 (CA).

¹⁶³ *Ibid.* See also *Prest v Petrodel Resources Ltd* [2013] UKSC 34 at para 21.

¹⁶⁴ Cassim (2013) 535 *De Rebus* 35 at 36.

4.2 The approaches to piercing the corporate veil in a group of companies

4.2.1 *Conservative approach*

South African jurisprudence demonstrated much earlier the will to ignore the separate personality of individual companies in the group framework. However the more recent conservative trend by the English courts demonstrated in *Adams v Cape Industries*,¹⁶⁵ wherein the courts decided against the corporate veil piercing and viewing the companies in a group as a single economic unit has been recognized in subsequent South African judgments.¹⁶⁶ The reasoning in *Wambach v Maizecor Industries*¹⁶⁷ for refusing corporate veil piercing was that an asset owned by the subsidiary company was not owned by the holding company, the respondent in this case, and therefore the respondent didn't have any right to it.

The stricter, conservative view holds that courts are not entitled to disregard the separate legal personality of a company in a group simply because it is just to do so. This was clearly suggested in *Adams v Cape Industries*¹⁶⁸ where it was stated that the court is not permitted to disregard the principle of the decision of *Salomon v Salomon*¹⁶⁹ merely because it considers that justice so requires apart from cases which turn on the wording of particular statutes or contracts. It was stated in *Salomon* as follows: "Our law for better or worse recognises the creation of subsidiary companies, which though in one sense are the creatures of their parent companies, will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities".

4.2.2 *Liberal approach*

In *Ebrahim v Airports Cold Storage*¹⁷⁰ the court compared our approach to those of the English courts when dealing with a case in which sections 64(1) and 65 of the Close Corporations Act¹⁷¹ had been invoked. The SCA upheld the court a *quo's* findings about

¹⁶⁵ *Adams v Cape Industries plc* [1991] 1 All ER 929 (CA).

¹⁶⁶ See *Wambach v Maizecor Industries (Edms) Bpk* 1993 (2) SA 669 (A), at 675D-E and *Macadamia Finance BK en 'n Ander v De Wet en Andere NNO* 1993 (2) SA 745 (A), at 748B-D. See also Cassim (2013) 535 *De Rebus* 35 at 36.

¹⁶⁷ *Wambach v Maizecor Industries (Edms) Bpk* 1993 (2) SA 669 (A).

¹⁶⁸ *Adams v Cape Industries plc* [1991] 1 All ER 929 (CA).

¹⁶⁹ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

¹⁷⁰ *Ebrahim v Airports Cold Storage (Pty) Ltd* 2008 (6) SA 585 (SCA).

¹⁷¹ Close Corporations Act 69 of 1984. Section 64(1) provides that "If it at any time appears that any business of a corporation was or is being carried on recklessly, with gross negligence or with intent to defraud any person or for any fraudulent purpose, a Court may on the application of the Master, or any creditor, member or liquidator of the

the appellants' (defendants in court a *quo*) reckless business and trading methods. The SCA found that the appellants conducted their business with no regard of statutory requirements; that they had no conception of, nor respect for, the fact that the Close Corporation was a distinct legal entity with a separate legal existence; and that they showed reckless disregard for the Close Corporation's capacity to accumulate assets of its own.

On the other hand, unlike in the United Kingdom where it appears corresponding provisions have been used very seldom in recent years to hold directors personally accountable, our courts witnessed a number of claimants who strongly relied on the provision.¹⁷² The general rule is that a company or corporation is a legal entity separate from its members or shareholders.¹⁷³ Therefore, although a decision to disregard a corporate personality or a finding of recklessness against a company is never arrived at lightly or for flimsy reasons or considerations, should such a decision be justified it would benefit or help maintain good corporate governance.¹⁷⁴

The corporate veil may be pierced where companies in a group can be regarded as associates. In *DHN Food Distributors v Tower Hamlets London Borough Council*¹⁷⁵ there were three companies which operated as a group and were recognised as a single economic unit on the basis that the holding company should be compensated for loss of its business under a compulsory acquisition order, although the land was owned by a subsidiary company. It was held that the companies should not be treated separately so as to be defeated on a technical point. It was therefore held that DHN as the holding company was entitled to compensation for disturbance of its business.¹⁷⁶

corporation, declare that any person who was knowingly a party to the carrying on of the business in any such manner, shall be personally liable for all or any of such debts or other liabilities of the corporation as the Court may direct, and the Court may give such further orders as it considers proper for the purpose of giving effect to the declaration and enforcing that liability. Section 65 provides that Whenever a Court on application by an interested person, or in any proceedings in which a corporation is involved, finds that the incorporation of, or any act by or on behalf of, or any use of, that corporation, constitutes a gross abuse of the juristic personality of the corporation as a separate entity, the Court may declare that the corporation is to be deemed not to be a juristic person in respect of such rights, obligations or liabilities of the corporation, or of such member or members thereof, or of such other person or persons, as are specified in the declaration, and the Court may give such further order or orders as it may deem fit in order to give effect to such declaration."

¹⁷² *Ebrahim v Airports Cold Storage (Pty) Ltd* 2008 (6) SA 585 (SCA).

¹⁷³ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at note 25.

¹⁷⁴ *Ibid* at 449.

¹⁷⁵ *DHN Food Distributors Ltd v Tower Hamlets London Borough Council* [1976] 1 WLR 852.

¹⁷⁶ Cassim *FHI et al* (2012) 54.

Recent case law suggests existence of judicial approach or philosophy that under the common law the separate personality of companies ought to be ignored only in exceptional circumstances or distinctive conditions and as a remedy of last resort.¹⁷⁷ However, there is no consistency of principle in the law or instances under which courts may disregard this principle of the separate personality of a company by lifting or piercing the veil of a company found to be a mere puppet or agent of its controllers.¹⁷⁸ It, therefore appears that, it would not be proper to enforce the principle of separate personality if the results would be “fragrantly opposed to justice, convenience or interests of the Revenue”.¹⁷⁹

4.2.3 *Realist Approach*

The realists view the corporation, although consisting of different individuals, as a living organism with its own objective reality.¹⁸⁰ The corporation is viewed as not a fiction but a real person in an extra legal sense with its own mind, will and body.¹⁸¹ In the decision of *Hulse-Reutter v Godde* the court adopted an approach that was much stricter and held that piercing the corporate veil should be used applied only as a remedy of last resort.¹⁸² The court in *Amlin SA v van Kooij*¹⁸³ agreed with this approach and stated that opening the curtains or piercing the veil is somewhat a drastic remedy, and therefore it must be used as a last resort especially where it will not be just to do so for parties. Piercing can therefore not be used as an alternative remedy where another remedy can be applied on the same facts.¹⁸⁴

A corporate veil is not capable of physical measurement, just like the corporation is not capable of being subjected to acts of touching or handcuffing or hard labour.¹⁸⁵ The legal existence of the corporate veil depends on it having some realistic justification and cause or some purpose capable of recognition, and practically, its existence is confirmed by grounds based on rational facts justifying it and proffering reasons or purpose for its being

¹⁷⁷ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 449.

¹⁷⁸ *Ibid.*

¹⁷⁹ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 449.

¹⁸⁰ Pretorius J T *et al* (1999) 9.

¹⁸¹ *Ibid.*

¹⁸² Cassim F H I *et al Contemporary Company Law* (2012) 49.

¹⁸³ *Amlin (SA) Pty Ltd v Kooij* 2008 (2) SA 558 (C).

¹⁸⁴ *Ibid* at para 23. See also Cassim F H I *et al* (2012) 49-50.

¹⁸⁵ Capuano A *The Realist guide to piercing the corporate veil: Lessons from Hong Kong and Singapore* (2009) 23 Australian Journal of Corporation Law 56 at 61. See further *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at note 8.

or existence.¹⁸⁶ Be that as it may, there is a view that the realists deny the existence of corporate veil.¹⁸⁷

An excessively inflexible or rigid approach to piercing the corporate veil of a company can result in unreal and formal application of law or “unreality and formalism”.¹⁸⁸ The appellate division in *Cape Pacific v Lubner Controlling Investments*¹⁸⁹ held that a more flexible approach which would allow the facts of each case to determine whether piercing the corporate veil is necessary or not should be adopted other than a more rigid approach which supports piercing the corporate where there is improper conduct.¹⁹⁰

4.3 Conclusion

Although greatly limited, the grounds upon which the corporate veil may be lifted reflect the “entrenched judicial attachment to formalist legal doctrine commonly noticeable in judgments on the subject”.¹⁹¹ The common law doctrine of piercing the corporate veil is an approach available to courts, but it has not been developed to an extent as to be the central legal strategy for redressing abuses of limited liability.¹⁹²

It is recommended that what is needed to pierce the veil, in addition to control, is an act of wrongdoing on the part of the parent company, either through its own actions or through the actions of the board of the subsidiary that it controls.¹⁹³ It is therefore proper to ignore the separate personalities of companies in a group and hold the parent company liable for activities of subsidiaries, if it is established that the group is operated in a manner that makes it difficult to distinguish between individual companies.¹⁹⁴

¹⁸⁶ *Supra* note 185.

¹⁸⁷ Capuano (2009) 23 *Aust Jnl of Corp Law* 56 at 61. See further *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at note 8.

¹⁸⁸ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 448.

¹⁸⁹ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 805.

¹⁹⁰ Cassim FHI *et al* (2012) 49.

¹⁹¹ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 448. This applies also in South Africa and England, and not only in Australia.

¹⁹² Davies PL (2016) 206.

¹⁹³ Anderson H *Piercing the corporate veil on corporate groups in Australia: The case for reform* (2009) 33 *Melbourne University Law Reform* 333, at 336.

¹⁹⁴ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 448.

CHAPTER 5: PIERCING OF THE CORPORATE VEIL IN A GROUP OF COMPANIES

5.1 Introduction and background

The term group of companies may be applied to companies linked together as holding and subsidiary companies or may also be applied to companies related as a result of having the same directors or controlled by the same individual.¹⁹⁵ As discussed above, a group of companies means a holding company and all its subsidiaries.¹⁹⁶ Holding company in relation to a subsidiary, means a juristic person that controls that subsidiary as a result of any circumstances contemplated in the Act.¹⁹⁷ A juristic person is related to another juristic person if either of them directly or indirectly controls the other; either is a subsidiary of the other; or a person directly or indirectly controls each of them, or the business of each of them.¹⁹⁸

The purpose for defining the holding/subsidiary company relationship was to form the basis for disclosure in financial position of a company and its subsidiary(ies) by way of group annual financial statements and to prevent the abuse of its control by a holding company over its subsidiary.¹⁹⁹ A possible abuse of control problem could arise where a holding company uses a subsidiary and its directors to compel the subsidiary to act to its own detriment.²⁰⁰

The basic characteristic of a group is that the management of different and independent holding and subsidiary companies making up a group is that they are managed on a central and unified basis in the interest of the group as a whole.²⁰¹ This management is

¹⁹⁵ Pretorius TJ *et al* (1999) 428.

¹⁹⁶ Section 1 of Act 71 of 2008.

¹⁹⁷ See sections 2(2)(a) and 3(1)(a). In terms of section 2(2)(a) of the Act, a person controls a juristic person, or its business if in the case of a juristic person that is a company, that juristic person is a subsidiary of that first person as determined in terms of section 3(1)(a); or that first person together with any related or inter-related person, is directly or indirectly able to exercise or control the exercise of a majority of the voting rights associated with securities of that company whether pursuant to a shareholder agreement or otherwise; has the right to appoint or elect, or control the appointment or election of, directors of that company who control a majority of the votes at a meeting of the board; or the first person has the ability to materially influence the policy of the juristic in a manner comparable to a person who in ordinary commercial practice, can exercise an element of control referred to above.

¹⁹⁸ Section 2(1)(c) of the Companies Act 71 of 2008.

¹⁹⁹ Botha DH (1981) 12.

²⁰⁰ Pretorius JT *et al* (2000) 434-435.

²⁰¹ Botha DH *Recognition of the group concept in Company Law* (1982) 15 De Jure 107 at 108. See also Cassim FHI *et al* (2012) 194.

possible because of the control inherent in the holding-subsidary company relationship which the holding company exercises over the subsidiary or subsidiaries.²⁰² However, the exercise of control by a holding company over its subsidiary does not result *per se* in the negation of the subsidiary's legal personality.²⁰³ Further, courts have made it clear that there is no separate independent *persona* apart from the *personae* of independent constituent companies comprising a group, and there are no interests involved except the interests of the group. However, no one could regard the group as having interests distinct from those of the different companies and the controllers.²⁰⁴

The control mentioned above led to the development of legislation necessary to regulate the group structure as the common law did not make provision for groups of companies.²⁰⁵ Accordingly, in accounting, group accounts are required to be prepared by the holding company and laid before its annual general meeting; accounting periods of the holding and subsidiary companies must be the same; and the auditor of a holding company has a right of access to all current and former financial statements of its subsidiaries.²⁰⁶ These disclosure provisions treat a group as an economic unit or business entity, although they do not operate to deny the separate legal personality of the different holding and subsidiary companies.²⁰⁷ It is thus clear that the principle of a group of companies being an entity separate from its constituent companies is applied differently in various disciplines.²⁰⁸

5.2 Fiduciary duties of directors in a group of companies

Each company in a group is a separate legal entity and the directors of a particular company are not entitled to sacrifice the interests of that company.²⁰⁹ The formation of company groups, especially the holding company's ability to control the subsidiary, subjects directors who are required to be independent organs of the subsidiary to more strain.²¹⁰

²⁰² *Ibid.*

²⁰³ Botha DH (1981) 70.

²⁰⁴ *R v Milner and Erleigh* 1951 (1) SA 791 (A) at 827. See also Cassim FHI *et al* (2012) 196.

²⁰⁵ *Ibid.* See also Cassim FHI *et al* (2012) 195.

²⁰⁶ Pretorius JT *et al* (1999) 421-422. See also *DHN Food Distributors Ltd v Tower Hamlets London Borough Council* (1976) 1 WLR 852 where the judge held that group of companies are treated as one concern for purposes of general accounts, balance sheet, and profit and loss account.

²⁰⁷ Botha DH (1981) 70.

²⁰⁸ Pretorius JT *et al* (1999) 428.

²⁰⁹ *Ibid.*

²¹⁰ Botha DH (1981) 70.

The general rule is that the fiduciary duties of a director are owed only to his own company. Where a director of a subsidiary is also a director of the holding company he, when acting as director of such subsidiary, still has the same fiduciary duty towards such subsidiary, as well as where the board of that subsidiary seeks to act in the interest of the group as a whole.²¹¹ Likewise, a holding company's director owes a fiduciary duty to a subsidiary where he deprived the nominees of all discretion until it is impossible for them to exercise an independent judgment.²¹²

In *Robinson v Randfontein Estate Gold Mining*,²¹³ the Appellate Division refused to recognise the separate legal personality of a subsidiary where Robinson had attempted to use the subsidiary as a device to evade the fiduciary duties he owed to the holding company as a director of that company. The judge stated that 'a man who procures the election of a board of directors under the circumstances which make it impossible for them to exercise an independent judgment, must observe the utmost good faith in his dealings with the company, which he has, purposefully, deprived of independent choice.²¹⁴ This is practice in cases where control is exercised over the policy and affairs of various companies by some controlling authority through nominee directors.²¹⁵ By disregarding the separate legal personality of the subsidiary company the court prevented Robinson from evading his fiduciary duties to the holding company.²¹⁶

As discussed above in 2.2.3 the director in a subsidiary company is placed in a position where there is a potential conflict between his fiduciary duty to the subsidiary and his interest, due to the fact that he is subject to the instructions from the holding company's directors, who through the holding company can control him. The fiduciary duties of directors of a subsidiary are thus of special significance for the protection of its shareholders and creditors where a group exists.

It appears that there is a need for liability of directors of a holding company in circumstances where they have destroyed the initiative of a subsidiary's board.²¹⁷ This is

²¹¹ See a similar statement in *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168.

²¹² Botha DH (1981) 227.

²¹³ *Robinson v Randfontein Estate Gold Mining Co. Ltd* 1921 AD 168 at 197.

²¹⁴ *Ibid.* See further Botha DH (1981) 228.

²¹⁵ *Ibid.*

²¹⁶ *Robinson v Randfontein Estate Gold Mining Co. Ltd* 1921 AD 168. See also Cassim FHI *et al* (2012) 43.

²¹⁷ Botha DH (1981) 228.

mostly the case as the directors of the holding companies are usually identified as the controllers of the subsidiary's directors.²¹⁸

5.3 Liability of companies in a group of companies

The general principles pertaining to piercing the corporate veil were applied in *Cape Pacific v Lubner Controlling Investments*²¹⁹ and the judge there held, amongst others, that a court would be justified in certain circumstances in disregarding a company's separate personality in order to fix liability elsewhere for what are supposedly acts of the company.²²⁰ The focus therefore shifts from the company to the natural person behind it, as if, there was no separation between such person and the company,²²¹ and as such personal liability shifts to someone who misuses or abuses the principle of corporate personality.²²²

Equally a holding company can be held liable for the acts, contract or delict, of the subsidiary thereby ignoring the separate corporate entity and shifting liability.²²³ This can be set out in two categories, namely, general legal principles encompassing the general principle of agency or estoppel, and the doctrine of instrumentality.²²⁴ As regards the doctrine of instrumentality the following requirements should be met, namely: control of the subsidiary by the holding company, use of control over the subsidiary by the holding company to commit fraud, dishonesty or an unjust act or to act in breach of a duty; and proximate causation of the damage/loss by the act of the holding company.²²⁵

In terms of the principle of agency a subsidiary is treated as a separate entity, but regarded in an inverted manner as the agent of its holding company.²²⁶ On the other hand a subsidiary can always act as agent of its holding company as authorised under an express agreement.²²⁷ The holding company will be bound by the acts of the agent as long as those acts are within the scope of the authority.²²⁸

²¹⁸ *Ibid.*

²¹⁹ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A).

²²⁰ Pretorius TJ *et al* (1999) 31. *Supra* note 105.

²²¹ *Ibid.*

²²² Pretorius TJ *et al* (1999) 31.

²²³ Pretorius TJ *et al* (1999) 429.

²²⁴ *Ibid.*

²²⁵ *Supra* note 223.

²²⁶ Botha DH (1981) 82-83.

²²⁷ *Ibid.*

²²⁸ Davies PL (2016) 203.

In *Salomon v Salomon*²²⁹ it was stated that the law on when a court may disregard the principle of separate legal personality by lifting the corporate veil and regarding the company as a mere agent or puppet of its controlling shareholder or parent corporation, follows no consistent principle. It was further stated that the best that can be said is that the separate entities principle is not enforced when it would yield a result too brazenly opposed to justice, convenience or the interests of entities like the Revenue authorities.

In *DHN Food Distributors v Tower Hamlets London Borough Council*²³⁰ the issue amongst others was whether DHN the holding company had an equitable interest in the land acquired by Bronze Ltd its wholly owned subsidiary; and whether the court was entitled to pierce the corporate veil which regarded limited companies as separate legal entities and treat the group as a single economic entity for the purpose of awarding compensation for disturbance. The court held that DHN had equitable interest it acquired all shares in Bronze; and further held that in many respects companies in a group are treated together as one concern for the purpose of general accounts, balance sheet, and profit and loss.²³¹

5.4 Conclusion

The judge stated in DHN Food Distributors case that there is evidence of a general tendency to ignore the separate legal personalities of companies in a group especially when a holding company owns all the shares of a subsidiaries, so much so, that it can control the activities of subsidiaries.²³² These subsidiaries are said to be bound hand and foot to the parent company and must do just what the parent company says.²³³

²²⁹ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

²³⁰ *DHN Food Distributors Ltd v Tower Hamlets London Borough Council* [1976] 1 WLR 852.

²³¹ Botha DH (1981) 75-76. See also discussion in 4.2.2 above.

²³² *DHN Food Distributors Ltd v Tower Hamlets London Borough Council* [1976] 1 WLR 852 at 860.

²³³ *Ibid.*

CHAPTER 6: PIERCING OF THE CORPORATE VEIL IN TERMS OF THE COMPANIES ACT 71 OF 2008

6.1 Introduction

The legislature sometimes sanctions the disregard of the principles regarding the separate corporate personality of a company, and this often happens in cases where the legislature renders persons other than the company liable for the debts of the company as a sanction for non-compliance with a statutory provision.²³⁴ The general principle of piercing the corporate veil is now codified in the Act, but is supplemental to, rather than substitutive of, the common law in respect of piercing (or lifting) the corporate veil.²³⁵

Section 20(9) of the New Companies Act²³⁶ created a statute-based ground for piercing or lifting the corporate veil of companies.²³⁷ This section provides a court with powers to disregard the juristic personality of a company, if on application by an interested person or in any proceedings in which a company is involved, a court finds that the incorporation of the company, any use of the company, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity. The questions now are under what circumstances and to what extent can a court apply this section, as opposed to the common law where piercing the corporate veil is to be used as a last resort.

6.2 Discussion of Section 20(9) of the Companies Act 71 of 2008

The legislature brought in section 20(9) in the companies legislation to give the aggrieved parties a platform, to protect investors and creditors, and thereby protect the assets of the company.²³⁸ The section offers interested parties an opportunity to approach the court and gives the courts a general statutory discretion to pierce the corporate veil.²³⁹

²³⁴ Cilliers HS *et al* (2000) 11.

²³⁵ Delport PA *et al* (2014) 100(3).

²³⁶ Section 20(9) of the Companies Act 71 of 2008.

²³⁷ *Ex Parte Gore NO and Others NNO* [2013] 2 SA 437 (WCC) at 451.

²³⁸ *Ibid.*

²³⁹ Cassim (2013) 535 *De Rebus* 35.

However, the term “interested person” is not defined in the Act.²⁴⁰ In the case of *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO en ‘n Ander*²⁴¹ the phrase an “interested person” was explained with reference to the use of the term in section 65 of the Close Corporations Act,²⁴² and it was held that the term should not be interpreted too restrictively and at the same time not too wide to an extent of including indirect interest. The interest, it was further held, should be limited to financial or monetary interest.²⁴³ For example, a creditor of a close corporation would be an interested person and may bring an application in terms of section 65 of the Close Corporations Act. The content of section 65 is similar to that of section 20(9) and therefore the interpretation of section 65 could offer some guidance, in determining who an interested person is, in an application in terms of section 20(9).

The term “unconscionable abuse” is also not defined in the Act. In terms of section 20(9) the juristic personality will be ignored and therefore the veil pierced when there’s a form of abuse by the controllers on the incorporation and the subsequent use of the company, and also abuse as a result of any act by, or on behalf of the company.²⁴⁴ In *Botha v Van Niekerk*²⁴⁵ the court held that it will pierce the corporate veil when the plaintiff has suffered some unconscionable injustice as a result of improper conduct on the part of the defendant.

In *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO*,²⁴⁶ a member of the close corporation was found to have acted fraudulently and recklessly, and as such the member’s actions constituted a gross abuse of the juristic personality. The court did not explain the term “unconscionable abuse”. The difference between “abuse” and “injustice” is that the term “injustice” refers to the consequences of the act, while the term “abuse” refers to the conduct that gives rise to the remedy.²⁴⁷

In the English case of *Ben Hashem v Ali Shayif*²⁴⁸ the court laid out the definition of unconscionable abuse as being whenever the illegitimate use of a juristic person

²⁴⁰ Act 71 of 2008.

²⁴¹ *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO en ‘n Ander* 1998 (1) SA 971 (O).

²⁴² Act 69 of 1984.

²⁴³ *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO en ‘n Ander* 1998 (1) SA 971 (O) at 986.

²⁴⁴ Cassim FHI *et al* (2012) 59.

²⁴⁵ *Botha v Van Niekerk* 1983 (3) SA 513 (W).

²⁴⁶ *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO en ‘n Ander* 1998 (1) SA 971 (O).

²⁴⁷ Delpont PA *et al* (2014) 100 (3).

²⁴⁸ *Ben Hashem v Ali Shayif and Another* [2008] EWHC 2380.

adversely affect a third party in a way that reasonably cannot be tolerated, that's unconscionable.²⁴⁹ The term unconscionable abuse of a juristic personality of a company suggests conduct in relation to the formation and use of companies diverse enough to cover all the descriptive terms like sham, device, stratagem and the like, used in the earlier cases, and the current cases, illustrates conceivably much more.²⁵⁰

A company which carries on its business recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose, may be required to show cause why its business or trading should not be ordered to cease by the Commission.²⁵¹ If a company fails to satisfy the Commission that it is not engaged in prohibited conduct, the Commission may issue a notice to require the company to cease carrying on with its business or trading.²⁵² This is usually the case where there is abuse of the juristic personality. Actions which show scant regard for the separate entities of companies will also amount to recklessness and, therefore, possible liability in terms of section 22 of the Act, which is another statutory basis for piercing the corporate veil.²⁵³

The consequence of a court declaring a company not to be a juristic person is that the separate legal personality of a company will terminate in respect of certain rights, obligations and liabilities.²⁵⁴ The Appellate Division in *Cape Pacific v Lubner Controlling Investments*²⁵⁵ emphasised that the corporate veil cannot be disregarded by a court whenever it considers it just to do so, but a court should rather strive to give effect to and uphold the company's separate personality. Therefore, section 20(9) should be interpreted with intention to preserve the company's separate legal personality, as opposed to supporting policy consideration in favour of piercing the corporate veil. The scope of the provision seems to extend the foundation upon which the courts in this country, have previously been prepared to grant relief that entails disregarding the corporate personality.²⁵⁶ Paragraph (b) of section 20(9) affords the courts the widest of powers to grant consequential relief. An order made in terms of paragraph (b) of section

²⁴⁹ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 452.

²⁵⁰ Delpont PA *et al* (2014) 100(3).

²⁵¹ See section 22 of the *Companies Act* 71 of 2008. The Companies and Intellectual Property Commission can in this regard issue a compliance notice to a company trading fraudulently.

²⁵² Delpont PA *et al* (2014) 104.

²⁵³ Delpont PA *et al* (2014) 100(3).

²⁵⁴ Cassim FHI *et al* (2012) 62.

²⁵⁵ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd and Others* 1995 (4) SA 790 (A) at 805. See also Cassim FHI *et al* (2012) 62.

²⁵⁶ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 451.

20(9) will always have the effect of fixing the right, obligation or liability somewhere else. In *Ex Parte Gore*,²⁵⁷ the right involved the property held by the subsidiary companies in the King Group and the obligation or liability is that which any of them might actually have to account to and make payment to the investors.

6.3 The solvency and liquidity of companies on distribution

Section 4 of the Act deals with solvency and liquidity test. A company satisfies the solvency and liquidity test at a particular time if, considering all reasonably foreseeable financial circumstances of the company at that time, the assets of the company, as fairly valued, equal or exceed the liabilities of the company, as fairly valued.²⁵⁸ As a restriction on distribution, a solvency test entails that the assets of the company should exceed its liabilities after the distribution has been taken into account.²⁵⁹

The regulation of distributions in the group context should be limited to instances where a subsidiary makes a distribution to shareholders of its holding company, and it should be made clear whether the financial restrictions will in such a case be applied independently to the subsidiary and the holding company, to the subsidiary and holding company as a unit, or to the group as a whole.²⁶⁰ On the other hand, if a holding company buys shares in an existing subsidiary or writes off a debt of that subsidiary, the transaction is also a distribution.²⁶¹ If the company is a member of a group of companies, the aggregate assets of the company, as fairly valued, must equal or exceed the aggregate liabilities of the company, as fairly valued.²⁶² Distributions may thus be made out of net assets only.²⁶³ Solvency in the sense of an excess of assets over liabilities is often referred to as solvency in the bankruptcy sense and is determined through a balance sheet test.²⁶⁴ Unlike the solvency element, which seems to refer to the financial position

²⁵⁷ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC).

²⁵⁸ Section 4(1). In terms of this section it must also appear that the company will be able to pay its debts as they become due in the ordinary course of business for a period of 12 months after the date on which the test is considered; or in the case of a distribution, 12 months following that distribution.

²⁵⁹ Van der Linde K *The Solvency and Liquidity approach to Companies Act 2008* (2009) 2 TSAR 224 at 225.

²⁶⁰ Van der Linde (2009) 2 TSAR 224 at 228. Section 1 provides that a distribution is a direct or indirect transfer by a company of money or other property of the company, other than its own shares, to or for the benefit of one or more holders of any such shares, of that company within the same group of companies, as consideration for the acquisition by any company within the same group of companies, of any shares of a company within that group of companies.

²⁶¹ Delport PA (2011) 59.

²⁶² Van der Linde (2009) 2 TSAR 224 at 227.

²⁶³ *Ibid.*

²⁶⁴ Van der Linde (2009) 2 TSAR 224 at 225.

of a group of companies, the liquidity element does not apply in the group context, but only to individual companies.²⁶⁵

The solvency and liquidity test must be based on a fair valuation of the company's assets and liabilities.²⁶⁶ In addition to this compulsory consideration of a fair valuation, the board or other person applying the test, may consider any other valuation of the company's assets and liabilities that is reasonable in the circumstances.²⁶⁷

A company should be prohibited from proceeding with a distribution if the directors are no longer satisfied that the company's financial situation allows it.²⁶⁸ The solvency and liquidity test is therefore an appropriate restriction on distributions to shareholders and a suitable protection measure in other transactions that may adversely affect the interests of creditors.²⁶⁹

6.4 Personal liability of directors

A director must not use his position or any information obtained while acting in the capacity of a director to gain an advantage for himself, or for another person, other than the company or a wholly-owned subsidiary of the company or to knowingly cause harm to a company or a subsidiary of the company.²⁷⁰ This duty implies that the director of the holding company has fiduciary duties towards the subsidiary company as well.²⁷¹ This is an extension from the common law position. In terms of the common law a director only owes fiduciary duties to the holding company and not the subsidiary company.²⁷² The general principle is therefore that each company in a group of companies should be regarded as a separate legal entity, unless the court pierces the corporate veil or it is done by the legislator.²⁷³

Where a director of a company acts without authority by engaging in reckless trading in the name of the company for fraudulent purposes, the director may be liable for any loss,

²⁶⁵ Van der Linde (2009) 2 *TSAR* 224 at 229.

²⁶⁶ Section 4(2)(b)(i). See also Van der Linde (2009) 2 *TSAR* 224 at 231.

²⁶⁷ Section 4(2)(b)(ii). See also Van der Linde (2009) 2 *TSAR* 224 at 231.

²⁶⁸ Van der Linde (2009) 2 *TSAR* 224 at 239.

²⁶⁹ *Ibid.*

²⁷⁰ Section 76(2) of the Companies Act 71 of 2008.

²⁷¹ Delpont PA *et al* (2014) 290(7).

²⁷² *Ibid.*

²⁷³ *Supra* note 271.

damages or costs sustained by the company as a direct or indirect consequence of the director's actions.²⁷⁴ However, if it appears to the court that the director is or may be liable, but has acted honestly and reasonably and having regard to all the circumstances of the case, it would be fair to excuse the director.²⁷⁵ The court would relieve the director, either wholly or partly, from the liability on any terms as the court considers just.²⁷⁶

6.5 Case study: *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC)

In *Ex Parte Gore*²⁷⁷ there was dishonesty and chaos in the administration of the affairs of a group of companies called the King Group, and the liquidators of the companies were unable to identify the relevant corporate entities against which the individual investor creditors had claims. The essential basis for the application was the allegation that the affairs in the King Group were conducted in a manner that didn't maintain any distinguishable corporate identity between the various companies in the group. In effect, there was no distinction between that company's legal personality and that of its subsidiaries. The question before the court was whether it should in this circumstances pierce the corporate veil and disregard the separate corporate personality of the various subsidiary companies, so that the assets of the subsidiary companies could be regarded as the assets of the holding company, for purposes of the investors' claims. The improprieties in dealing with the investors' funds involved the use of the companies to conceal the true facts. The relevant improprieties involved the controllers of the companies treating the group in a way that drew no proper distinction between the separate personalities of the constituent members and in using the investors' funds in a manner that is inconsistent with what had been represented. The conduct of the business of the group of companies with scant regard for the separate legal personalities of the individual corporate entities of which it was comprised, would in itself constitute a gross abuse of the corporate personality of all the entities concerned. The court decided then that in terms of section 20(9), subsidiary companies, except for King Financial Holdings Limited, the holding company, be deemed not to be juristic persons in respect of any obligation by such companies to the individuals or entities that had invested in the King companies. The court held further that the King companies shall be regarded as a single

²⁷⁴ See section 77(3)(a) to (d).

²⁷⁵ Delport PA et al (2014) 304(2).

²⁷⁶ *Ibid.*

²⁷⁷ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC). See also Cassim (2013) 535 *De Rebus* 35 on a discussion of *Ex Parte Gore* case.

entity; their separate legal existence be ignored and the holding company be treated as the only company.²⁷⁸

6.6 Conclusion

The principle of piercing the corporate veil as codified in the Act, complements rather than substitute the common law in respect of piercing (or lifting) the corporate veil.²⁷⁹ Interested parties can approach the court in terms of Section 20(9) which also offers the courts a general statutory discretion to pierce the corporate veil.²⁸⁰

This section should be interpreted with intention to maintain the company's separate legal personality, as opposed to supporting policy consideration in favour of piercing the corporate veil.²⁸¹ The corporate veil cannot therefore be disregarded by a court whenever it considers it just to do so, but a court should rather strive to give effect to and uphold the company's separate personality.²⁸²

The provisions of section 20(9) (defined in a very flexible manner) has created a firm basis for determining issues relating to the concept and effectively dealt away with the belief or philosophy that caution ought to be applied in piercing the corporate veil²⁸³ or that it be considered a remedy of last resort in terms of the common law. The section provides a remedy when justified or dictated by the facts of the case and as such makes the remedy readily available, as opposed to the notion that it only provides relief in exceptional or drastic circumstances.²⁸⁴ Consequently the unqualified availability of the remedy in terms of the statutory provision also weighs against an approach that the remedy should be granted only in the absence of any alternative remedy.²⁸⁵ Section 20(9) is therefore a remedy that can be applied even where other remedies exist.²⁸⁶

²⁷⁸ *Ibid.*

²⁷⁹ Delpont PA *et al* (2014) 100(3).

²⁸⁰ Cassim (2013) 535 *De Rebus* 35.

²⁸¹ Cassim FHI *et al* (2012) 62.

²⁸² *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd and Others* 1995 (4) SA 790 (A) at 805. See also Cassim FHI *et al* (2012) 62.

²⁸³ *Ex Parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 452.

²⁸⁴ *Ibid.*

²⁸⁵ *Ex Parte Gore NO and Others NNO* at 452-453.

²⁸⁶ Cassim (2013) 535 *De Rebus* 35.

CHAPTER 7: FOREIGN LAW AND JURISDICTION / LEGAL COMPARISON

7.1 Introduction and background

The legal structure of modern business was born out of a century old principle of the separate juristic personality established by *Salomon v Salomon*,²⁸⁷ which protects shareholders' private assets by limiting their liability in case of claims against the corporate. The *Salomon* case²⁸⁸ had more influence on the South African company law, and was thus referred to in most court decisions and is still applicable.²⁸⁹

The issue to be determined in most authorities referred to in this review is whether or not, and if so, in what circumstances, the court has power to pierce the corporate veil. The answer to this question is discussed in paragraph 7.2, hereunder.

7.2 Development of piercing the corporate veil in foreign law

7.2.1 English Law

Lord LJ stated in *VTB Capital v Nutritek International Corp*²⁹⁰ that veil piercing is about substance not form. It was held that any doctrine permitting the court to pierce the corporate veil must be limited to cases where there was a relevant impropriety.

In *Adams v Cape Industries*²⁹¹ the court held that the corporate veil could be disregarded only in cases where it was used for the deliberately dishonest purpose. It was held further that the court is not free to disregard the principle of *Salomon v Salomon* merely because it considers that justice so requires.

In *Merchandise Transport v British Transport Commission*,²⁹² it was held that where the characters of a company, or the nature of the persons who control it, is a relevant feature, the court will go behind the mere status of the company as a legal entity, and will consider

²⁸⁷ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

²⁸⁸ *Ibid.*

²⁸⁹ *Botha v Van Niekerk* 1983 (3) SA 513 (W); *Ex Parte Gore NO v Others NNO* [2013] 2 All SA 437 (WWC).

²⁹⁰ *VTB Capital plc v Nutritek International Corp* [2012] EWCA Civ 808 at para 87.

²⁹¹ *Adams v Cape Industries plc* [1991] 1 All ER 929 (CA).

²⁹² *Merchandise Transport Ltd v British Transport Commission* [1962] 2 QB 173.

who are the persons, as shareholders or even as agents, who direct and control the activities of a company which is incapable of doing anything without human assistance.²⁹³ As regards companies group, the House of Lords held in *Lonrho Ltd v Shell Petroleum Co Ltd*,²⁹⁴ that documents of a subsidiary were not in the power of its parent company for the purposes of disclosure in litigation, simply by virtue of the latter's ownership and control of the group.

The group phenomenon has been mostly recognised in financial reporting where a true and fair view of overall position of the company is to be presented and that, accordingly, when one controls others, the parent company must present group financial statements, as well as, its own individual statements, thus avoiding the misleading impression which the latter alone might give.²⁹⁵

In *Prest v Petrodel*,²⁹⁶ the issue was whether or not, and if so, in what circumstances, the court has power to pierce the corporate veil in the absence of specific statutory authority to do so. It was stated by Lord Neuberger that it is clear from the cases and academic articles that the law relating to the doctrine is unsatisfactory and confused. The cases and articles, it was stated further, appear to suggest that (i) there is no single instance in the United Kingdom jurisdiction where the doctrine has been invoked properly and successfully, (ii) there is doubt as to whether the doctrine should exist, and (iii) it is impossible to discern any coherent approach, applicable principles, or defined limitations to the doctrine.²⁹⁷ Lord Neuberger mentioned with evidence that there is lack of any coherent principle in the application of the doctrine.²⁹⁸

7.2.2 Australian Law

In *Gorton v Federal Commissioner of Taxation*,²⁹⁹ Windeyer J remarked that an unduly rigid approach to piercing the corporate veil could lead the law into unreality and formalism.

²⁹³ *Ibid* at 206.

²⁹⁴ *Lonrho Ltd v Shell Petroleum Co Ltd* [1980] 1 WLR 627.

²⁹⁵ Davies PL (2016) 231-232.

²⁹⁶ *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

²⁹⁷ *Ibid* at para 64.

²⁹⁸ *Prest v Petrodel Resources Ltd* at para 75.

²⁹⁹ *Gorton v Federal Commissioner of Taxation* (1965) 113 CLR 604.

Trending in the opposite direction however, Hill J in the Federal Court commented in *AGC (Investments) Ltd v Commissioner of Taxation (Cth)*³⁰⁰ and stated that the circumstances in which the corporate veil may be lifted are greatly circumscribed, thus reflecting the entrenched judicial attachment to formalist legal doctrine commonly discernible in judgments on the subject not only in Australia, but also in England and South Africa.

In their article analysing the approach of the Australian courts to piercing the corporate veil, Ramsay and Noakes identify group enterprises as one of five categories of factors that might lead to a decision to pierce the veil.³⁰¹ They further identify that it is a factor that is evident in cases which indicate that a corporate group is operating in such a manner as to make individual entity indistinguishable and therefore it is proper to pierce the corporate veil to treat the parent company as liable for the acts of the subsidiary.³⁰²

In *Briggs v James Hardie & Co Pty Ltd*,³⁰³ Rogers AJA observed that there is no common, unifying principle, which underlies the occasional decision of courts to pierce the corporate veil, and that there is no principled approach to be derived from the authorities. It is recommended that what is required to pierce the veil in holding/subsidiary relationship, in addition to control, is an act of wrongdoing on the part of the parent company, either through its own actions or through the actions of the board of the subsidiary that it controls.³⁰⁴

In Australia corporate groups or groups of companies are said to have much in common with directors and closely held companies, and many of the same reasons for piercing the corporate veil in companies apply to corporate groups.³⁰⁵ Further, the directors' duties to act with care and diligence and in good faith were suggested as the model of liability for parent companies facing piercing of the corporate veil.³⁰⁶

7.3 Conclusion

As appearing above, in the United Kingdom the courts have been prepared to disregard

³⁰⁰ *AGC (Investments) Ltd v Commissioner of Taxation (Cth)* (1992) 92 ATC 4239.

³⁰¹ Ramsay (2001) 19 *Company and Securities LJ* 250.

³⁰² *Ibid*

³⁰³ *Briggs v James Hardie & Co (Pty) Ltd* (1989) 16 NSWLR 549, 567.

³⁰⁴ Anderson (2009) 33 *Melbourne University Law Reform* 333 at 336.

³⁰⁵ *Ibid* at 367.

³⁰⁶ Anderson (2009) 33 *Melbourne University Law Reform* 333 at 337.

the separate legal entities of the various holding and subsidiary companies in a group and have, for certain purposes, treated them as one economic entity.³⁰⁷ However, the cases have not worked out what is meant by 'piercing the corporate veil',³⁰⁸ although there is consensus in most authorities that there are circumstances in which the court may pierce the corporate veil.³⁰⁹

Further, in Australia, the courts will only pierce the veil if the corporate form has been used for fraud, to shield the parent company from an existing legal obligation (the 'sham/ façade' basis) or for corporate groups, where the level of control 'is so complete that [the parent company] is deemed to be directly liable for activities' of the subsidiary.³¹⁰

Although, South African courts have often referred to a group, they have never regarded a holding company and its subsidiary(ies) as constituting a separate independent *persona* apart from the *personae* of the independent constituent companies comprising a group. The South African courts influenced by the decision in *Salomon's* case emphasised the separate legal personality and interests of the different holding companies and subsidiaries.

On a consideration of South African, English and Australian jurisprudence, it is clear that the courts' willingness to pierce, lift, or look behind the corporate veil has significantly varied, upon circumstances of each case over the years.³¹¹

³⁰⁷ Cilliers HS *et al* (2000) 14.

³⁰⁸ [2013] UKSC 34 para 75.

³⁰⁹ *Ibid* para 26.

³¹⁰ Anderson (2009) 33 *Melbourne University Law Reform* 333 at 354.

³¹¹ *Ex parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 444.

CHAPTER 8: CONCLUSION

This research evaluated the extent of powers which the courts have in order to pierce the corporate veil of a company in particular a company in a group of companies. The statutory provisions, mainly section 20(9) of the Companies Act 71 of 2008 (the Act), which gives the courts the widest power to pierce the corporate veil, and also common law, were considered in the evaluation.

As discussed in paragraph 2.1.1 above, a company is considered a juristic person from the date and time of registration and such registration bequeaths the company with a separate legal or juristic personality. Any activities of the company are thus for the company only and not its members. The definition of juristic personality outlines a scope of when the circumstances of a particular case make it appropriate for courts to disregard it by piercing the corporate veil, which veil creates a protective shield to members of a company from external interference. However, the protection is limited under certain circumstances and can be ignored if those circumstances are justifiable.

The circumstances providing guidance and justification to disregard juristic personality of a company as a separate juristic entity, were developed in common law. Whether, piercing the veil can be used either as a last resort or not and when circumstance so dictate, is a question which most judges in South Africa and other jurisdictions tackled with caution. At common law, the remedy of piercing the corporate veil is used as a last resort.³¹² The principle developed in *Salomon v Salomon*, which principle is still instructive in courts, where there is an issue about whether to disregard the separate legal personality or not, is that a legally incorporated company must be treated like any other independent person with its rights and liabilities appropriate to itself and not its members.³¹³

Piercing the corporate veil is therefore used broadly to describe the distinct occasions where there is an exception to the principle of the separate juristic personality of a company, reiterated in *Salomon v Salomon*.³¹⁴ These occasions may result from a statutory provision, or from joint liability in tort or delict, or from the law of unjust

³¹² *Hülse-Reutter and Others v Gödde* 2001 (4) SA 1336 (SCA) para 23. Cassim FHI *et al* (2012) 58.

³¹³ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

³¹⁴ *Prest v Petrodel Resources Ltd* [2013] UKSC 34 at para 106. See also *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

enrichment, or from principles of equity and the law of trusts.³¹⁵ However, the circumstances in which it would be permissible to pierce the corporate veil seem far from settled with regard to the separate legal personality of a company and those who control it. Moreover, it appears to have been recognised that proof of fraud or dishonesty might justify disregarding the separate corporate personality.³¹⁶ Further, South African authorities show that courts will ignore or look behind the separate legal personality of a company where justice so requires, and not only when there is no alternative remedy, despite the repeated affirmation that the courts enjoy no general discretion to pierce the corporate veil merely because it would be just and equitable to do so.³¹⁷ In most cases where the principle of separate legal personality was ignored, fraud or improper conduct was established or proved as the basis.³¹⁸

The introduction of section 20(9) of the Act makes provision for courts to pierce the corporate veil in instances where unconscionable abuse is established. Aggrieved parties, like investors and creditors, are afforded protection as interested parties and may approach the courts in terms of section 20(9) relief regarding the protection of the company assets³¹⁹ by way of veil piercing.

A court can extend the application of the doctrine of piercing the corporate veil to apply to a group of companies, as if they are a single entity and thereby piercing the veil of the holding company and ignoring separate legal personalities of the other subsidiary companies in a group.³²⁰

On whether the assets and liabilities of a company, as a member of a group, should be taken into account together with that of the group, the solvency test as discussed in chapter 6 is applied mostly on distribution in company groups. The test entails that the assets of the company should exceed its liabilities after the distribution has been taken into account.³²¹ A company is therefore prohibited from proceeding with a distribution if

³¹⁵ *Prest v Petrodel Resources Ltd* [2013] UKSC 34 at para 106.

³¹⁶ *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 803.

³¹⁷ *Ex parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 450.

³¹⁸ *Ibid.*

³¹⁹ Cassim (2013) 535 *De Rebus* 35.

³²⁰ *Ibid* at 36.

³²¹ Van der Linde (2009) 2 *TSAR* 224 at 239.

the company's financial situation does not allow it.³²² The solvency and liquidity test is a protective measure provided for in the Act to secure the interests of creditors.

The circumstances for piercing the corporate veil in a group of companies, as developed in the decision of *Ex Parte Gore*, established a precedent illustrating to directors, shareholders and controllers of companies that the corporate veil will be pierced where unconscionable abuse of the juristic personality of the company is found, including company groups, and that the remedy will not be regarded as an exceptional one to be used only as a last resort.³²³ This is re-assuring to third parties/investors interested in understanding the activities of a company and the scope of liability of the shareholders in company.

However, there is no "common, unifying principle" grounding, from time to time, decisions of the courts to pierce the corporate veil by the courts.³²⁴ While a court of law will always have a reason for any decision made, there is no consistency of legal principles or the approaches adopted discernable from the authorities to piercing the veil in companies.³²⁵ On the other hand, whilst the doctrine of piercing the corporate veil has been available as a legal remedy under common law, it is very limited in extent, due to lack of development, to significantly redress all forms of abuse of limited liability.³²⁶

³²² *Ibid.*

³²³ *Supra* note 320.

³²⁴ *Amlin (SA) Pty Ltd v Van Kooij* 2008 (2) SA 558 (C). See also *Briggs v James Hardie & Co (Pty) Ltd* (1989) 16 NSWLR 549 (NSWCA) and *Ex parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 444.

³²⁵ *Ex parte Gore NO and Others NNO* [2013] 2 All SA 437 (WCC) at 444.

³²⁶ Davies PL (2016) 206.

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