EXAMINATION OF CIRCUMSTANCES WHEN THE CORPORATE VEIL WILL BE PIERCED

Submitted in partial fulfillment of the requirements for the degree LLM in Corporate Law by

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22 November 2019

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CHAPTER 1: INTRODUCTION

1.1 Introduction

Companies are juristic persons which have a separate legal personality.[1] They are creatures of statute,[2] as they have, in the words of Lord Chancellor Baron Thurlow 'no soul to damn and no body to kick'.[3] A company cannot perform acts on its own but has to rely on its agents – that is; directors, shareholders and other office bearers.[4] It nevertheless has the capacity to acquire rights and responsibilities which are different from its agents. This is what entails the principle of the separate legal personality of a company.[5]

One of the fundamental consequences of companies having a separate legal personality is that they operate on the principle of limited liability.[6] Limited liability, in Cassim's words, means that "the liability of shareholders for the company's debts is limited to the amount they have paid to the company for its shares. The shareholders are as a general principle not liable for the debts of the company."[7]

In principle, it is the shareholders and not the company which enjoys limited liability, as the company is liable for all the debts that it incurs.[8] Shareholders are only liable for claims against the company only as far as their capital contribution".[9]

The principles of separate legal personality and limited liability have not been strictly applied by the courts, as there are instances where the courts have disregarded the separate legal personality of a company or a group of companies and treated the company and shareholders as one, with the result that the shareholders became liable

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[1] *Salomon v Salomon Co Ltd* [1897] AC 22; see also Bourne, J. 'Lifting the corporate veil' (2002) *Juta's Business Law* at 114.
[2] *Ebrahim v Airport Cold Storage (Pty) Ltd* 2008 (6) SA 585 (SCA) at 15.
[3] *Salomon v Salomon Co Ltd* [1897] AC 22; see also Farouk HI Cassim *et al Contemporary Company Law* 2ed (2012) at 28.
[4] *Ibid.*
[5] *Ibid*; see also section 19(1)(b) of the Companies Act 71 of 2008.
[6] *Salomon v Salomon Co Ltd* [1897] AC 22 at 44.
[7] Farouk HI Cassim et al *Contemporary Company Law 2ed* (2012) at 31-32.
[8] *Supra* note 7 at 32.
[9] *Supra* note 6 at 35.

for claims against the company.[10] This is referred to as piercing of the corporate veil, which implies that the court '"opens the curtain" of the corporate entity in order to see for itself what obtained inside'.[11]

In a group of companies, there are cases where the corporate veil was pierced, with the result that the holding company became liable for claims against the subsidiary.[12] In other cases, courts have rejected piercing of the corporate veil in a group of companies.[13] Cassim states that

> "this difficulty is more acute in the context of groups of companies, where the courts have been divided in their approach whether, and in what circumstances, the corporate veil may be pierced so that the group is in fact treated as a single entity as opposed to a collection of different corporate entities."[14]

The problem which exists regarding the remedy of piercing the corporate veil is the way in which it has been inconsistently applied on principle, with the result that there continues to be uncertainty regarding the circumstances when the courts will disregard the separate legal personality of a company.[15]

The Companies Act[16] has codified piercing of the corporate veil through section 20(9). In Ex *Parte Gore*,[17] it was stated that this section does not replace the common law. This essentially means that there now exist two remedies for piercing of the corporate veil in South Africa. The provisions of the sections are however not clearly defined, presenting interpretational difficulties.

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[10] *Ritz Hotel Ltd v Charles of the Ritz Ltd* 1988 3 SA 290 A; *DHN Food Distributors Ltd v London Borough of the Tower Hamlets* [1976] 3 ALL ER 462; David K. Millon "Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability" *Emory L. J.* 1305 (2007) at 1325.
[11] *Supra* note 7 at 38.
[12] *DHN Food Distributors Ltd v London Borough of the Tower Hamlets [1976] 3 ALL ER 462*; *Ex Parte Gore* [2013] 2 All SA 437 (WCC).
[13] *Adams v Cape Industries plc* [1991] 1 ALL ER 929 (CA).
[14] Rehana Cassim "Hiding behind the veil" (2013) *De Rebus* 36.
[15] Rehana Cassim "Piercing the veil under section 20(9) of the Companies Act 71 of 2008" 2014 *SA Mercantile Law Journal* 307; *Hülse-Reutter v Gödde* 2001 (4) SA 1336 (SCA) at 20.
[16] 71 of 2008 ('the Act').
[17] [2013] 2 All SA 437 (WCC).

1.2 Problem-statement

The fundamental problem which triggers the necessity of this research, is the uncertainty regarding circumstances when the courts will pierce the corporate veil. This uncertainty arises due to the way the courts have inconsistently applied principles regarding piercing of the corporate veil.[18]

The above-mentioned uncertainty has been stressed on multiple occasions by the courts and various authors.[19] In *Ex Parte Gore*, it was stated that there are no clearly defined principles upon which the courts may use to determine whether to pierce the corporate veil.[20] This view, reflected in *Ex Parte Gore*,[21] receives support from Lord Neuberger, who, in *VTB Capital Plc v Nutritek International Corp & Ors*[22] stated that

> "The notion 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."[23]

In *Cape Pacific Ltd v Lubner controlling Investments*[24] it was stated that "the law is far from settled in regards to the circumstances in which it will be permissible to pierce the corporate veil."[25]

1.3 Purpose of the study

The purpose of this study is two-fold. Firstly, it aims to examine the circumstances in which the courts have disregarded the separate legal personality of companies.

[18] *Infra* notes 19, 20 and 21.
[19] *Supra* note 7; *supra* note 15.
[20] *Supra* note 17 at 19.
[21] *Idem* at 20.
[22] [2013] UKSC 5.
[23] *Idem* at 123.
[24] *Cape Pacific Ltd v Lubner controlling Investments Ltd* 1995 (4) SA 790 (A).
[25] *Idem* at 28.

Secondly, it seeks to provide guidelines regarding how piercing of the corporate veil, as a remedy, should be applied by the courts. These guidelines extend to the interpretations of the provisions of section 20(9) of the Act.

1.4 Limitations of this dissertation

The research in this study is limited to the position of the law as of 30 October 2019.

1.5 Research questions

The following questions will be dealt with:

1. What does separate legal personality and limited liability mean?

2. When can courts pierce the corporate veil under common law?

2.1 What approach have the courts adopted?

2.2 In which instances have the courts pierced the corporate veil?

2.3 Do the courts consider piercing of the corporate veil as a remedy of last resort?

3. How does section 20(9) of the Act approach piercing of the corporate veil?

3.1 What constitutes an 'interested person'?

3.2 What does 'unconscionable abuse' mean?

3.3 Is section 20(9) a remedy of last resort?

3.4 Does section 20(9) replace common law piercing of the corporate veil?

4. How have the courts applied the remedy of piercing the corporate veil in a group of companies?

5. How have the courts approached piercing of the corporate veil in England and Australia?

1.6 Methodology

This study uses a qualitative literature research methodology. Primary and secondary sources are used as points for critical engagement. A comparative study is undertaken

regarding how the courts have pierced the corporate veil in the United Kingdom and Australia. The primary reason why these jurisdictions have been chosen is because the South African courts, when rationalizing whether to pierce the corporate veil, have consistently considered the rationale in the mentioned jurisdictions.[26]

1.7 Structure of the mini dissertation

Chapter 1: Introduction.

Chapter 2: Separate legal personality and common law piercing of the corporate veil.

Chapter 3: Piercing of the corporate veil in terms of section 20(9) of the Companies Act 71 of 2008.

Chapter 4: Piercing of the corporate veil in a group of companies

Chapter 5 Comparative study of piercing the corporate veil in the United Kingdom and Australia.

Chapter 6 Conclusion and recommendations.

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[26] *Supra* note 24 at 29.

CHAPTER 2: SEPARATE LEGAL PERSONALITY AND COMMON LAW PIERCING OF THE CORPORATE VEIL

2.1 Introduction

This chapter firstly provides an analysis of the concepts of separate legal personality and limited liability. Secondly, it outlines the development of the common law remedy of piercing the corporate veil. The discussion is on the various approaches which have been adopted by the courts when considering whether to disregard the separate legal personality of a company.

The argument is that the flexible approach laid down in *Cape Pacific Ltd v Lubner controlling Investments*[27] is comparatively more beneficial than the categorizing approach as found in *Botha v Van Niekerk*.[28]

An analysis is provided as to whether piercing of the corporate veil in common law is a remedy of last resort. It is submitted that piercing of the corporate veil should not be a remedy of last resort despite the availability of an alternative remedy.

2.2 Separate Legal Personality and Limited Liability

The principle of the separate legal personality of a company was entrenched in *Salomon v Salomon.*[29]

2.2.1 Principles laid down by the court

The court laid the foundation of what constitutes a company's separate legal personality and its subsequent relations to the principle of limited liability. Lord Halsbury L.C elaborated that the separate legal personality of a company means that the company should be viewed like any other independent person, with the result that it acquires rights which it can enforce and obligations which can be enforced against it.[30]

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[27] *Supra* note 24.
[28] *Botha v Van Niekerk en 'n Ander* 1983(3) SA 513(W).
[29] *Supra* note 7.
[30] *Idem* at 30.

Lord Macnaghten states that one of the consequences of a company having a separate legal personality is that the company and its members operate on the principle of limited liability.[31] He further explains that limited liability means that the liability of the members of a company is limited with respect to the debts of the company and that this is different to a situation of partners, where their liability would be unlimited.[32]

Lord Macnaghten further notes that the liability of a shareholder in a company would be limited by only the amount that the shareholder paid.[33] The benefit of limited liability is that one shares in the profit of a company without taking on the risk of being liable for the company's debts.[34]

2.3 Analysis of the nature and consequences of separate legal personality

2.3.1 Capacity to own property

In *Dadoo Ltd v Krugersdorp Municipal Council*[35] the principle of a company's separate legal personality was expanded upon. The legal issue raised was whether a company has the capacity to own property in its own name. Prior to deciding this legal issue, the court reiterated that the separate legal personality of a company is "no merely artificial and technical thing"[36].

Wessels, J in the court *a quo* of the *Dadoo v Krugersdorp Municipal Council* case, the judge stated that:

> '"f we fix our eyes too much upon its corporate existence and its being a legal entity we are apt to lose sight of the fact that after all a company is only a partnership of individuals who have obtained the sanction on the state to act as a juristic person."[37]

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[31] *Idem* at 44.
[32] *Ibid*.
[33] *Idem* at 35.
[34] *Ibid*.
[35] *Dadoo Ltd v Krugersdorp Municipal Council* 1920 AD 530.
[36] *Idem* at 550.
[37] *Idem* at 536.

The argument by Wessels, J puts forward the idea that the separate legal personality of a company is a technical phenomenon which, in the judge's view, does not correlate with the practical "fact" that a company is a collective of individuals.

This constitutes a direct contrast to the principle of a company's separate legal personality, as laid down in *Salomon v Salomon* as well as the appellate division in *Dadoo v Krugersdorp Municipal Council* , as in the two mentioned cases, it is required for one to think of the company as an independent person instead of a collective of individuals.[38]

In the appellate division of the *Dadoo v Krugersdorp Municipal Council* case; it is argued, by implication, that since a company has a separate legal persona, it has the capacity to own property in its own name, that such property belongs to the company itself and not to the company's shareholders or any other members of the company.[39]

It is important to distinguish between the financial interest that a shareholder has in the assets of a company and the right to those assets. In *Stellenbosch Farmers' Winery Ltd v Distillers Corporation (SA) Ltd*[40] it was held, with respect to distributions, that a shareholder's financial interest to the company's assets does not mean that shareholder has any right or title to the company's assets.[41]

It is held further in this case that the profits which a company makes forms part of the assets of that company.[42] In outlining the evidence that a shareholder has a financial interest in a company, the court held that:

> "The fact that the shareholder is entitled to an *aliquot* share in the distribution of the surplus assets when the company is wound up proves that he is financially interested in the success or failure of the company but not that he has any right or title to any assets of the company."[43]

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[38] *Supra* note 28 and note 34.
[39] *Supra* note 35 at 550-551.
[40] 1962 (1) SA 458 (A).
[41] *Idem* at 472.
[42] *Idem* at 489 – 490.
[43] *Ibid*.

In *Macaura v Northern Assurance Co Ltd*[44] Macaura sold timber estate to a company in which he is a shareholder and creditor. The timber was insured against fire in Macaura's own name and not the name of the company. When the timber was destroyed by fire, the insurance company refused to pay, contending that the property that was destroyed belonged to the company and not to Macaura.[45]

The House of Lords agreed with the argument of the insurance company on the basis that Macaura, as shareholder or creditor of the company, does not have any rights to the assets of the company.[46]

2.3.2 Limited liability

Limited liability, to borrow from Cassim's words, "means the liability of shareholders for the company's debts is limited to the amount they paid to the company for its shares."[47] It is however important to note that it is the shareholders and not the company which enjoys limited liability.[48] Creditors can only claim against the company, they cannot claim from the assets of shareholders what they are owed by the company.[49]

The practical purpose served by limited liability, as argued by Cassim, is that it encourages investors to invest in businesses because their risk is limited. These investments subsequently help businesses to grow their finances and operations.[50]

2.3.3 Perpetual succession

The separate legal personality of a company allows for it to continue despite the death of its members or the transfer of shares of the company.[51]

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[44] [1925] AC 619 (HL)(Lr)).
[45] *Supra* note 7 at 34.
[46] *Supra* note 44 at 630; *Supra* note 7 at 34.
[47] *Supra* note 7 at 31.
[48] *Supra* note 7 at 32.
[49] *Ibid*.
[50] *Ibid*.
[51] *Ibid*.

2.3.4 Profits of the company belong to the company

A shareholder cannot claim rights to the profits of a company. It is the company which owns the profits. A shareholder only has a right to the company's profit when dividends have been declared by that company.[52]

In *S v De Jager*[53] a shareholder and director of a public company used the company's profits for personal use, which was not in the best interest of the company. The court stated that such an act amounts to theft, given that property which belonged to the company was taken by a shareholder for personal use.

The argument raised by the accused is that both the shareholder and director agreed to the distribution of the profit. The court held that this argument does not hold, as the agreement was done in breach of the director's fiduciary duties.[54] It held that

> "The appellant's contention is an attempt to have it both ways. On the one hand he would retain the advantage of limited liability as a shareholder. On the other hand he would seek to absolve himself from the fiduciary duty which a director owes to the company, helping himself to its assets *via* its supposed consent to which he was a party."[55]

The court placed further reliance on *Rex* v. *Milne and Erleigh*[56] in carrying forward the argument that "any person of ordinary intelligence" cannot believe that they have the power to despoil a company, particularly when that person has a fiduciary duty to that company.[57]

2.3.5 Debts of the company are owed by the company and not shareholders

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[52] *Supra* note 7 at 34.
[53] 1965 (2) SA 616 (A).
[54] *Supra* note 7 at 35.
[55] *S v De Jager* at 505.
[56] 1951 (1) S.A. (A.D.) 791.
[57] *Ibid*.

Shareholders are not accountable for the debts of the company, hence when a company is liquidated, the debts of the company cannot be recovered from shareholders' personal estate.[58]

In *JH Rayner (Mincing Lane) Ltd v Department of Trade and Industry*[59] it was held that for the limited liability enjoyed by shareholders to be set aside, creditors can try to negotiate for "adequate guarantees from members of the corporation or adequate security."[60]

2.3.6 Capacity to conclude contracts in its own name

A shareholder cannot enter into agreements on behalf of the company without authorization.[61]

In *Lee v Lee's Air Farming Ltd*[62] Lord Morris held that a person can serve in duel functions in the same company, for instance, in this case Lee was both a director and worker of the company.[63] In arriving to this conclusion, the court held that being a director of a company does not automatically prevent such a person from entering into a contract to serve that company.[64] Furthermore, Lord Morris relied on Lord Halsbury LC's view in *Salomon v Salomon* that a company is a real thing, with legal existence and consequently capable of entering into transactions as a result of acquiring rights and responsibilities.[65]

Lord Morris relied further on *Inland Revenue Comrs v Sansom.*[66] In this case, the company in question had authorized in its memorandum of incorporation for the granting of loans without security or interest. Sansom, as the company's director, concluded a loan agreement with the company. Lord Younger LJ held that for as long as a company's legal status is recognized, it can validly enter into contracts in its own name.[67]

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[58] *Supra* note 7 at 36.
[59] 1990 2 AC 418 HL.
[60] *Idem* at 521; *supra* note 7 at 36.
[61] *Supra* note 7 at 36.
[62] 1961 AC 12.
[63] *Supra* note 7 at 37.
[64] *Lee v Lee's Air Farming Ltd* 1961 AC 12 at 425.
[65] *Ibid*.
[66] [1921] 2 KB.
[67] *Lee v Lee's Air Farming Ltd* 1961 AC 12 at 427.

2.4 Common Law Piercing of the Corporate Veil

2.4.1 Approach

The debate of what approach a court should use when piercing the corporate veil has been subject to varying analysis and conclusions by the courts throughout the years. In *Hulse-Reutter v Godde*[68] it was held that a court does not have a general discretion to pierce the corporate veil despite consideration by that court that piercing of the corporate veil would be just or convenient.[69]

It is further argued in this case that the separate legal personality of a company ought to be preserved save for what the court terms as "unusual circumstances".[70] In *Amlin (SA) Pty Ltd v Van Kooij* the court goes as far as to pronounce that "South African courts are free to consider alternative approaches to piercing the corporate veil".[71]

2.4.2 Categorizing versus Flexible approach

The courts have pierced the corporate veil on various occasions.[72] In many such judgments, it is admitted that there exists uncertainty as to when the corporate veil should be pierced.[73]

2.4.2.1 Categorizing approach

A categorizing approach is an approach which puts in place only specific categories or circumstances when the corporate veil should be pierced.

In *Botha v Van Niekerk*[74] a categorizing approach was followed. In this case, it was held that the corporate veil will only be pierced where there is an "unconscionable injustice" which results from the abuse of the separate legal personality of a company.[75] It is argued

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[68] *Hulse-Reutter v Godde* 2001 (4) SA 136 (SCA).
[69] *Idem* at 20.
[70] *Ibid.*
[71] *Supra* note 22 at 21.
[72] *Ritz Hotel Ltd v Charles of the Ritz Ltd* 1988 3 SA 290 A; *DHN Food Distributors Ltd v London Borough of the Tower Hamlets* [1976] 3 ALL ER 462.
[73] *Supra* note 24 at 28.
[74] *Botha v Van Niekerk en 'n Ander* 1983(3) SA 513(W).
[75] *Ex Parte Gore* [2013] 2 All SA 437 (WCC) at footnote 36; in *Amlin v Van Kooij* at 21 it is argued that this specific judgment in Botha v Van Niekerk is obiter and that the courts are free to consider alternative approaches to piercing the corporate veil.

this ground of piercing is focused on the consequence of abusing the separate legal personality of a company.[76]

In *Lategan v Boyes*[77] it was held that the South African courts, much like the Canadian courts at the time, would only pierce the corporate veil only in the event where the company's separate legal personality was used for fraudulent purposes.[78] The court considered the *Orkin Bros Ltd v Bell*[79] case as precedence for piercing the corporate veil.[80] In the *Orkin Bros Ltd v Bell* case judgment was obtained against a director who was said to have committed fraud against the seller.[81]

2.4.2.2 Flexible approach

Cape Pacific Ltd v Lubner controlling Investments provides an analysis of the flexible approach.

In *Cape Pacific Ltd v Lubner controlling Investments,* it was held that each case should be judged on its own facts.[82] It thus rejects the categorizing approach to piercing the corporate veil. The court instead argues that a flexible approach would be more appropriate and that the rigid approach applied in *Botha v Van Niekerk*[83] should not be followed.[84] A flexible approach is one which allows the facts of that particular case to be a final determinant as to whether the corporate veil should be pierced.[85]

Cassim supports the flexible approach proposition in *Cape Pacific Ltd v Lubner controlling Investments*.[86] One of the main reasons advanced by Cassim is that should the categorizing approach be followed, there could be instances where piercing the corporate veil could be justified but fail on the grounds that such instances fall outside of the ambit

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[76] *Ibid*.
[77] 1980 (4) SA 191 (T).
[78] *Supra* note 72 at 201.
[79] 1921 TPD 92.
[80] *Idem* at 201.
[81] *Ibid*.
[82] *Idem* at 802.
[83] *Botha v Van Niekerk en 'n Ander* 1983(3) SA 513(W) at 524A.
[84] *Supra* note 24 at 37.
[85] *Ibid*.
[86] *Supra* note 7 at 46.

of the rigid categories.[87] I concur with Cassim, on the condition that there should be clearly defined principles and/or guidelines that assist the court in determining whether the corporate veil should be pierced. It would possibly bring more uncertainty in this area of the law if the determination of whether the corporate veil should be pierced is subject to the flexible approach without clear guiding principles.

2.4.3 Balancing approach

The *Cape Pacific Ltd v Lubner controlling Investments* case argues for the balancing approach when the court is faced with a question of whether to pierce the corporate veil.[88] This approach requires that there should be a balance between preserving the separate legal personality of a company against policy considerations in favour of piercing the corporate veil.[89]

In this case, when applying the facts, the court held that policy considerations "strongly suggest" that in instances of fraud or improper dealings for the purpose of evading legal obligations, the corporate veil should be pierced.[90]

Ex Parte Gore supports the balancing approach. It however classifies policy considerations as "the adverse moral and economic effects of countenancing an unconscionable abuse of the concept by the founders, shareholders or controllers of a company."[91]

In submission, the proposition of a balancing approach is supported. It is however important to highlight that whilst a balancing approach aligned with a flexible approach would arguably, on comparison, provide more effective outcomes than a categorizing approach, it is still a cause of concern that there are no guidelines as to how the policy considerations in favour of piercing the corporate veil ought to be identified and weighed. This admittedly still leaves a gap of uncertainty in this area of the law.

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[87] *Supra* note 7 at 45.
[88] *Supra* note 24 at 803.
[89] *Ibid*.
[90] *Supra* note 24 at 35; see also *The Shipping Corporation of India Ltd v Evdomon Corporation and Another* 1994(1) SA 550(A) at 566C-F.
[91] *Supra* note 24 at 29.

2.5 Instances of common law piercing

Cassim outlines instances where the corporate veil was pierced under common law; that is - when the separate legal personality of a company was used by directors to evade their fiduciary duties and where it was used to overcome a contractual duty.[92]

2.5.1 Evading Contractual Obligations

In *Gilford motors Co Ltd v Horne*,[93] which dealt with restraint of trade – a former managing director had agreed with the company for which he was a director that he will not engage in activities similar to the company's trade for five years. In attempting to overcome this obligation, the former directors started a company which engaged in the activities prohibited by the restraint of trade agreement.[94] The argument thereafter raised by the former managing director is that it is not him but the company, as a juristic person with a separate legal personality that is engaged in the prohibited activities.

The court rejected the former managing director's argument. It reasoned that the company was 'a device and a stratagem, a mere cloak and a sham' which the former managing director used in order to overcome the restraint of trade agreement.[95] This meant that the company was being used as an "instrument" by the former managing director.[96]

In *Le' Bergo Fashions CC v Lee*[97] the facts of the case were similar to the one in *Gilford Motors*, the only difference is that in the former case the company was already in existence.[98] The reasoning however differs in wording from the one in *Gilford Motors* as in the *Le'Bergo Fashions CC v Lee* it was held that

> "I am of the view that the factors relied upon by the applicant and enumerated above are sufficient to sustain the argument that the first

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[92] *Supra* note 7 at 40.
[93] *Gilford motors Co Ltd v Horne* 1933 Ch 935 (CA).
[94] *Supra* note 7 at 41.
[95] *Ibid*; see also *Le' Bergo Fashions CC v Lee* 1998 (2) SA 608 at 612; In *Adams v Cape Industries Plc v Cape Industries plc* [1991] 1 ALL ER 929 (CA) at 1023 it is stated that whenever an accusation arises that a company is carried on as a "device" or "sham" or "cloak" then the motive of the accused will be relevant.
[96] *Le' Bergo Fashions CC v Lee* 1998 (2) SA 608 (C) at 612.
[97] 1998 (2) SA 608 (C).
[98] *Supra* note 7 at 612.

> respondent is guilty of improper conduct in using her company, the second respondent, as a facade behind which she has engaged in business in breach of the restraint of trade undertaking."[99]

Le'Bergo Fashions CC v Lee relies on *Cape Pacific Ltd v Lubner controlling Investments*, in as far as whether it is relevant that the company was not started with a fraudulent purpose.[100] In *Cape Pacific Ltd v Lubner controlling Investments* it was held that it matters not whether the company was started with a fraudulent purpose or not, what matters is the substance behind a particular transaction.[101]

In the case of *Jones v Lipman*,[102] Lipman sold land to Jones but thereafter sought to avoid the agreement with Jones by transferring the land to a company which he formed for that purpose. This company was controlled by Lipman. The court disregarded the separate legal personality of the company, calling the company a "device" "sham" and "mask" which was used by Lipman.[103]

2.5.2 Separate legal personality used as a device by a director to evade his or her fiduciary duty

In *Robinson v Randfontein Estates Gold Mining Co Ltd*[104] it was held that a director may not use a company in order to evade his or her fiduciary duties to the company. In this case, the director tried to evade his fiduciary duty to the holding company through the use of a subsidiary company.[105]

2.6 Remedy of last resort

In *Cape Pacific Ltd v Lubner controlling Investments the* court argues that it does not, on principle, observe a basis upon which piercing of the corporate veil should be used as a remedy of last resort when an applicant has two available remedies.[106] The view it raises

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[99] *Supra* note 7 at 614.
[100] *Supra* note 7 at 615.
[101] *Supra* note 7 at 42.
[102] (1962) 1 ALL ER 442.
[103] *Supra* note 7 at 42.
[104] 1921 AD 168.
[105] *Supra* note 7 at 40.
[106] *Supra* note 24 at 37-38.

is that an applicant who has two available remedies has a choice to elect one remedy, even though in some circumstances a person may by bind by the election of that one choice.[107]

This court argues that when a court is faced with a matter concerning piercing of the corporate veil; the availability of another remedy or the failure to pursue that alternative remedy may be of relevance when it comes to policy considerations.[108]

The argument raised in *Cape Pacific Ltd v Lubner controlling Investments* contradicts the one in *Hulse-Reutter v Godde*, which clearly outlined that piercing of the corporate veil should be used as a remedy of last resort.[109] *Hulse-Reutter v Godde* concurs with *Amlin (SA) Pty Ltd v Van Kooij*[110].

The argument which *Hulse-Reutter v Godde* raises, in essence, is that piercing of the corporate veil is a 'drastic' remedy.[111] As such, such a remedy should only find application in exceptional circumstances.[112] The underlying argument appears to be that if a particular remedy is drastic, then it should not be readily available when a least drastic remedy is available.

Amlin (SA) Pty Ltd v Van Kooij, though by conclusion it agrees with *Hulse-Reutter v Godde,* the reasoning behind why piercing of the corporate veil should be used as a remedy of last resort is given a relatively different perspective. It is argued by this court that veil piercing as a remedy ought to be a last resort in the instance that "justice will not otherwise be done between the two litigants".[113]

There are two critical questions which arise from the line of argument presented in the *Amlin (SA) Pty Ltd v Van Kooij* case. The first question pertains to what constitutes "justice" between two litigants? This question bears significance as the court holds that if

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[107] *Ibid*.
[108] *Supra* note 24 at 40.
[109] *Supra* note 68 at 46.
[110] *Amlin (SA) Pty Limited v Van Kooij* 2008 (2) SA 558 (C).
[111] *Supra* note 7 at 46.
[112] *Ibid*.
[113] *Supra* note 110 at 23.

an alternative remedy is available that can administer justice between the two litigants, then piercing of the corporate veil should be used as a remedy of last resort.[114]

It is submitted contrary to *Hulse-Reutter v Godde* and *Amlin (SA) Pty Ltd v Van Kooij*, that piercing of the corporate veil should not be a remedy of last resort. A person who has two remedies may pursue one remedy over the other. Indeed, piercing of the corporate veil negates the separate legal personality of a company and it is 'drastic'. However, I am convinced that if an applicant pursues piercing of the corporate veil as a remedy, despite another remedy being available, what is of overriding importance is whether the courts apply sound principles in determining whether or not to pierce the veil. For as long as the courts apply the correct principles and a company's separate legal personality is disregarded, that would not amount to the courts undermining the principle. A drastic remedy such as this would be undermined where it was arbitrarily negated, that is, where no sound principles were used. It is a further submission, in line with the *Cape Pacific Ltd v Lubner controlling Investments* case, that the availability of another remedy may be a relevant factor when taking policy considerations into account, in line with the balancing approach.

2.7 Piercing the veil versus lifting the veil

There is a difference between the terms 'piercing the veil' and 'lifting the veil'. Much of the discussion thus far has centered around piercing the veil. Lifting the veil, on the other hand means that the court looks into who the shareholders and directors of the company are.[115]

Daimler Co Ltd v Continental Tyre and Rubber Co[116] serves as a classic example of lifting the veil. In 1914 there was a war between England and Germany. There existed a rule during that time that a company cannot trade with the enemy. In order to uphold this rule, the enemy character had to be determined. A company was established in England in

[114] *Ibid.*
[115] *Atlas Maritime Co SA v Avalon Maritime Ltd* [1991] 4 ALL ERR 769 at 779.
[116] [1916] 2 AC 307.

order to sell in that country tires which were made in Germany. The England-incorporated company was majority controlled by German citizens (as shareholders), save for one person who was a naturalized British albeit born in Germany. In order to determine whether the shareholders constituted enemy character, they looked behind the veil in order to determine who the shareholders were.[117]

2.8 Conclusion and recommendations

In this chapter, an analysis of the consequences that arise from the separate legal personality of a company was provided. The decision is *Salomon v Salomon*[118] as well as *Dadoo Ltd v Krugersdorp Municipal Council*[119] with respect to this principle were discussed, as well as other subsequent cases.

The common law remedy of piercing the corporate veil was also discussed. It is submitted, as part of recommendations, that the flexible and balancing approach as expressed in *Cape Pacific Ltd v Lubner controlling Investments*[120] should be followed.

When considering the issue of whether piercing of the corporate veil should be a remedy of last resort, it is submitted that the approach in *Cape Pacific Ltd v Lubner controlling Investments* should be followed.

[117] *Supra* note 7 at 43.
[118] *Supra* note 6.
[119] *Supra* note 35.
[120] *Supra* note 24.

CHAPTER 3: PIERCING OF THE CORPORATE VEIL IN TERMS OF SECTION 20(9) OF THE COMPANIES ACT 71 OF 2008.

3.1 Introduction

The Companies Act 71 of 2008 introduced a statutory provision of piercing the corporate veil through section 20(9) of the Act. Prior to the introduction of section 20(9), piercing of the corporate veil only existed as a common law remedy.

This chapter investigates whether section 20(9) of the Act serves as a welcome provision, when it comes to resolving some of the issues that existed under common law piercing of the corporate veil. Focus will be placed on whether the section settles the debate on piercing the corporate veil as a remedy of last resort, on the approach which the courts should follow as well as the grounds for piercing the corporate veil.

Three arguments are advanced, namely:

a) Section 20(9) of the Companies Act should not replace the common law remedy of piercing the corporate veil. This position is favourable as it widens the application of the remedy. In *Ex Parte Gore* it is stated that:

> "The introduction of the statutory provision has given rise to some debate on whether the subsection has replaced the common law on piercing the corporate veil. Certainly there is no express intention apparent to that effect, as for example to be seen in s 165(1) of the Act (concerning derivative actions), but, equally, there is no express indication that the intention is not to displace the common law, like that to be found in s 161(2)(b) (concerning remedies available to protect the rights of the holders of securities in companies)."[121]

b) In *Ex Parte Gore* the remedy was not considered a remedy of last resort considering its availability when the facts justify piercing of the corporate veil. This approach should be accompanied by the approach in *Cape Pacific Ltd v Lubner controlling Investments,*

[121] *Supra* note 17 at 31.

which states that the availability of another remedy or the failure to pursue it may be a relevant factor in policy considerations.

c) The provisions of section 20(9) provide uncertainty, bring about interpretational challenges and further guidelines need to be developed.

The provisions of Section 20(9) of the Companies Act 71 of 2008 are as follows:

> (9) 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 court may -
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> (a) declare that the company is to be deemed not to be a juristic person in respect of any right, obligation or liability of the company or of a shareholder of the company or, in the case of a non-profit company, a member of the company, or of another person specified in the declaration; and (b) make any further order the court considers appropriate to give effect to a declaration contemplated in paragraph (a).

3.2 The relationship between section 20(9) of the Act and common law piercing of the corporate.

In *Ex Parte Gore*, the court argues that section 20(9) expands on the common law principles of piercing the corporate veil.[122] There is no suggestion in the Act that section 20(9) of the Act replaces the common law. Cassim argues that the provisions of section 20(9) do not 'override' the common law instances of piercing the corporate veil.[123] The

[122] *Idem* at 32.
[123] *Supra* note 7 at 54.

author further suggests that when there can be no reliance on the statutory provisions then the common law provisions will find application.[124]

Consideration must be given to the approach of the Companies Act 71 of 2008, with reference to section 165 of the Act. This section is explicit in stating that the common law derivative no longer finds application due to the introduction of the statutory derivative action. Section 165(1) states that:

> Any right at common law of a person other than a company to bring or prosecute any legal proceedings on behalf of that company is abolished, and the rights in this section are in substitution for any such abolished right.

Section 20(9) does not provide any such language which is express or can be implied to abolish the common law remedy of piercing the corporate veil. It is likely that only in situations where the common law provisions clash with section 20(9) provisions then the statutory provisions will prevail.

Further reliance can be placed on section 158(a) of the Act, which obliges the court to develop the common law to the extent that the enjoyment and realizations of the rights contained in the Act are established.

A question which arises is whether the co-existence of section 20(9) as well as the principles of piercing the corporate veil under the common law would better serve the purpose of the Act. Should reliance only be placed on section 20(9) of the Act, there is a danger that a categorizing approach might be developed if the provisions are interpreted restrictively. As such, not abolishing the common law would serve the purpose of avoiding a situation where certain instances which might necessitate piercing of the corporate veil are excluded.[125] This avoidance, it is submitted, provides a comparatively better platform for the effective and responsible management of companies.

3.3 Whether it is a remedy of last resort

[124] *Ibid.*

[125] *Idem* at 55.

The provisions of section 20(9) do not resolve the question whether piercing of the corporate veil should be a remedy of last resort. In the common law, there has been a debate, with contradicting conclusions, as to whether piercing of the corporate veil should be a remedy of last resort. In *Hulse-Reutter v Godde*, the Supreme Court of Appeal concluded that it should be a remedy of last resort.[126] In *Cape Pacific Ltd v Lubner controlling Investments*, on the other hand, it was determined that it should not be used as a remedy of last remedy merely because another alternative remedy exists.[127]

In *Ex Parte Gore* the court argues that section 20(9) is not a remedy of last resort.[128] The argument raised by the court in this regard is two-fold. In the first instance, the court argues that section 20(9) has been made available without qualification.[129] This provides the opportunity to rely on the remedy if the facts of a particular case are consistent with the provisions of the section.[130]

Secondly, the court argues that the provisions of section 20(9) are not as drastic compared to the provisions of section 65 of the Close Corporations Act (similarly wording to section 20(9)) which require that there should be gross abuse.[131] Indeed, the court does not provide any justification as to why it considers unconscionable abuse to be of a lesser standard compared to gross abuse.[132]

In *Ex Parte Gore*, it is argued that "by expressly establishing its availability simply when the facts of a case justify it, the provision detracts from the notion that the remedy should be regarded as exceptional, or 'drastic'."[133]

Cassim argues that piercing of the corporate veil is an exceptional remedy which should not be used sparingly.[134] I submit that despite its availability, it is still a drastic remedy. As

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[126] *Hulse-Reutter v Godde* 2001 (4) SA 136 (SCA) at 23.
[127] *Supra* note 24 at 37-38.
[128] *Supra* note 7 at 35.
[129] *Ibid*.
[130] *Ibid*.
[131] *Ibid*.
[132] Zindoga, WT *Piercing of The Corporate Veil in Terms of Gore: Section 20(9) Of the New Companies Act 17 Of 2008* (LLM Dissertation 2015 UCT) at 44.
[133] *Supra* note 17 at 34.
[134] *Supra* note 7 at 55.

with *Ex Parte Gore* and *Cape Pacific Ltd v Lubner controlling Investments,* I submit that it should not necessarily be a remedy of last resort.

3.4 Interpretation of the provisions of section 20(9)

3.4.1 Meaning of interested person

The provisions of section 20(9) do not specify what constitutes an interested person. As such, case law on section 65 of the Close Corporations Act can be of interpretative value as it is similar in wording to section 20(9) in wording.

In *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis* NO[135] the court argued that interested person should neither be given a restrictive interpretation, nor should it be given an interpretation so wide such that it includes persons with an indirect interest. It settled by stating that it will suffice if a person has monetary or financial interest.[136]

In *Ex Parte Gore* it was concluded that reliance on interpretation of what constitutes an interested person should be placed on the already established principles from case law.[137] In this light, the court placed forward the case of *Jacobs en 'n Ander v Waks*.[138] It was furthermore stated in the case that section 38 of the constitution will be applicable were the Bill of Rights are of relevance.[139]

In *Jacobs en 'n Ander v Waks*, an interested person is considered as one who has a real, direct interest in the case and the interest should not be remote or abstract.[140] The determination of whether there is a direct interest in a particular case does not have fixed rules, leaving the court with discretionary powers given the circumstances of each case.[141]

It is submitted that the approach in *Jacobs en 'n Ander v Waks* should be followed. There would be drastic consequences should someone with a real, direct interest in a case

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[135] 1998 (1) SA 971 (O).
[136] *Supra* note 7 at 55.
[137] *Supra* note 17 at 35.
[138] 1992 (1) SA 521 (A).
[139] *Supra* note 17 at 35.
[140] Cassim, R. 'Piercing the veil under section 20(9) of the Companies Act 71 of 2008' (2014) *SA Mercantile Law Journal* at 312.
[141] *Supra* note 138 at 313.

which is not remote or abstract be denied an opportunity to bring an application in terms of section 20(9) of the Act.

3.4.2 Unconscionable abuse

The term 'unconscionable abuse' is not defined in the Act. It is uncertain whether it bears the same meaning as 'gross abuse' which is found in section 65 of the Close Corporations Act or whether different meanings can be attributed to both terms.

The word "unconscionable" within the context of piercing the corporate veil was first introduced in South Africa in *Botha v Van Niekerk*[142] where the term "unconscionable injustice" was used as the ground upon which the corporate veil should be pierced.[143] In that case, no clearly outlined definition is provided regarding what unconscionable means.

It is also questionable whether the terms unconscionable abuse and unconscionable injustice have the same meaning. 'Injustice' appears to suggest that it is the end result which should be looked into, thus in a case where there is a misuse of the separate legal personality of a company which does not result in any injustice there would be no need to pierce the corporate veil. Abuse on the other act appears to focus more on the act rather than the result, meaning that for as long as there was an act where the separate legal personality of a company was used, the remedy of piercing the corporate veil might be triggered even though there might not have been an 'injustice'.[144]

In *Hulse-Reutter v Godde* the analysis advanced was that the corporate veil would be pierced in a situation where there is an abuse of the corporate personality with the result that those who abused the corporate personality would receive an unfair advantage.[145]

On principle, the analysis by *Hulse-Reutter v Godde* is similar to the one by *Botha v Van Niekerk* in that both cases place an emphasis on a resultant effect of the abuse of the separate legal personality of a company. Section 20(9) on the other hand, does not make the remedy available on the ground that there should be a particular result which arises

[142] 1983 (3) SA 513 (W).
[143] *Supra* note 17 at 34.
[144] Supra note 17 at footnote 36.
[145] *Supra* note 7 at 56.

from abusing the company's separate legal personality. It merely requires that there should be an act which amounts to an unconscionable abuse of a company's separate legal personality.[146]

In *Ex Parte Gore* it was held that the term 'unconscionable abuse' is wide enough to cover words such as 'sham', 'device', 'stratagem', and 'conceivably much more'.[147] Cassim[148] states that

> "One might argue that on *Gore*'s interpretation of the pivotal words 'unconscionable abuse', just about any abuse of the juristic personality of a company would be unconscionable."[149]

Section 65 of the Close Corporations Act can serve as a guideline of interpreting what unconscionable abuse means. The section is worded as follows:

> 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.[150]

[146] *Ibid*.
[147] *Supra* note 17 at 34.
[148] Cassim, R. 'Piercing the veil under section 20(9) of the Companies Act 71 of 2008' (2014) *SA Mercantile Law Journal* 305.
[149] *Idem* at 318.
[150] Section 65.

Prior to investigating section 65 of the Close Corporations Act, it is worth noting, with difficulty, as to why the *Ex Parte Gore* case considered 'gross abuse' as being more 'extreme' than 'unconscionable abuse' when it stated that:

> "This much seems to be underscored by the choice of the words '*unconscionable abuse*' in preference to the term '*gross abuse*' employed in the equivalent provision of the Close Corporations Act; the latter term having a more extreme connotation than the former. The term 'unconscionable abuse of the juristic personality of a company' postulates 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 that connection in the earlier cases, and - as the current case illustrates - conceivably much more."[151]

In *Airport Cold Storage (Pty) Ltd v Ebrahim*[152] the court laid down the similarities between companies and close corporations in the development of the separate legal personality of a company. It stated that "one of the most fundamental consequences of incorporation is that a close corporation – just like a company – is a juristic entity separate from its members."[153]The court further outlined that this principle, also applicable to close corporations, finds its roots from the *Salomon v Salomon*[154] case.[155]

In *Mncube v District Seven Property Investments CC*[156] the court attempted to provide clarity as to what entails abuse of a juristic person's separate legal personality. It raised the proposition that it should entail using the separate legal personality of a juristic person for a 'nefarious purpose'. This proposition adds further complications in that it introduces

[151] *Supra* note 17 at 34.
[152] 2008 (2) SA 303 (C).
[153] *Supra* note 7 at 17.
[154] *Salomon v Salomon Co Ltd* [1897] AC 22.
[155] *Supra* note 152 at 17.
[156] [2006] JOL 17381 (D).

terms which come with interpretational difficulties on top of a term clouded with uncertainty. [157]

In *Haygro Catering BK v Van Der Merwe*[158] the name of the corporation was not reflected on any of its premises, documents or correspondences. This was in contravention of section 23 of the Close Corporation Act.[159] Section 23 dealt with the use and publication of close corporations' names. The contravention of section 23 was considered to be a gross abuse of the separate legal personality of the company.[160]

In *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO*[161] one of the members of a close corporate provided loans to a corporate with full knowledge that the corporation was insolvent.[162]The court highlighted that this amounts to gross abuse in violation of section 65 of the Close Corporations Act.[163]

In *Airport Cold Storage (Pty) Ltd v Ebrahim*[164] the court laid down factors which should be considered in determining whether there was a gross abuse of the separate entity of the company. The factors are as follows:

> "a) The close corporation had formed part of a conglomerate of associated family businesses that had been conducted with scant regard for the separate legal personalities of the entities concerned,
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> b) The close corporation had not kept proper books of account,
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> c) The close corporation had opened without having appointed an accounting officer,
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> d) The close corporation had voluntarily assumed a debt owing by the family business when it was incorporated and had acquired

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[157] *Supra* note 7 at 57.
[158] 1996 (4) SA 1063 (C).
[159] *Supra* note 7 at 57.
[160] *Ibid*.
[161] 1998 (1) SA 971 (O).
[162] *Supra* note 7 at 57.
[163] *Supra* note 7 at 58.
[164] 2008 (2) SA 303 (C).

> significant debts from the start of commencing business, which had amounted to reckless trading."[165]

3.5 Court orders

Once the court has pierced the corporate veil, it can provide that the company is deemed not to be a juristic person. This implies that the company and its members will not have some rights associated with the separate legal personality of a company.[166]

3.6 Conclusion

In this chapter, the provisions of section 20(9) of the Act were analyzed. It was submitted that section 20(9) does not override the common law remedy of piercing the corporate veil. Instead, the Act places an obligation on the courts to develop the common law where necessary, in order to ensure that the rights under the Act are realized.

It was submitted that the conclusion in *Ex Parte Gore*[167] that piercing of the corporate veil is not a remedy of last resort is correct.

The ground of "unconscionable abuse" expressed in section 20(9) does not have any clearly defined meaning. This is also the case with the term "interested person." It is submitted that the principles expressed in the *Jacobs en 'n Ander v Waks*[168] case should find expression in future cases, as they account for persons with a real, direct interest in the case, of which the interest is not remote.

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[165] *Supra* note 7 at 58.
[166] *Supra* note 7 at 59.
[167] *Supra* note 17.
[168] *Supra* note 135.

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

4.1 Introduction

In this chapter, an analysis of piercing the corporate veil in a group of companies will be provided. As will be seen, the courts have had differing conclusions regarding whether to pierce the corporate veil in a group of companies. The conservative and relaxed approached will be critically analyzed as well as the agency principle as reflected in *Smith, Stone & Knight Ltd v Lord Mayor, Aldermen Citizens of the City of Birmingham*.[169]

4.2 Definition of group of companies

Section 1 of the Act defines a group of companies as "a holding company and all of its subsidiaries." A holding company is defined in section 1 as "in relation to a subsidiary, means a juristic person that controls that subsidiary as a result of any circumstances contemplated in section 2(2)(a) or 3(l)(a)."

4.3 Conservative approach

In *Reitz Hotel Ltd v Charles of the Ritz Ltd*[170] It was held that the holding and subsidiary company are two separate entities each with its own separate legal personality. It therefore means that the acts of the holding company cannot be considered to be the acts of the subsidiary company.[171]

In *Adams v Cape Industries Plc*[172] it was held that courts do not have the discretion to disregard the separate legal personality of group companies even though that court "considers that justice so requires."[173] It re-emphasized that one of the benefits that arise with having groups of companies that have a separate legal personality is the assurance that one company can avoid liability that arises due to the acts of another company, it stated this as follows:

[169] [1939] 4 ALL ER 116.
[170] 1988 (3) SA 290 A.
[171] *Idem* at 314.
[172] [1991] 1 ALL ER 929 (CA).
[173] *Idem* at 1019.

> "The purpose of the operation was in substance that Cape would have the practical benefit of the group's asbestos trade in the United States of America without the risks of tortious liability. This may be so. However, in our judgment, Cape was in law entitled to organize the group's affairs in that manner and ... to expect that the court would apply the principle of *Salomon v Salomon* & Co. Ltd . . .. in the ordinary way."[174]

The court in *Adams v Cape Industries plc* nevertheless agrees with Lord Keith in *Woolfson v Strathclyde Regional Council*[175] when he (Lord Keith) argued that on principle the corporate veil can only be pierced in the instance where there is a mere façade concealing the true facts.[176]

In *Ord v Belhaven Pubs Ltd*[177] the court rejected the idea of a group of companies being a single economic unit. It stated that this principle can only be relaxed in the instances where there was "some impropriety or the company was a façade concealing the true facts."[178]

In *Wambach v Maizecor Industries (Edms) Bpk*[179] the board of directors of the holding company were the same as that of the subsidiary company. They could control the movement and use of assets of the subsidiary company. The court rejected piercing of the corporate veil and maintained that both companies have a separate legal personality despite having the same directors.[180]

In *Macadamia Finance Bpk v De Wet*[181] the directors of the holding company were the same as that of the subsidiary company. The property of the subsidiary company was destroyed. In argument, the subsidiary company claimed that the holding company was

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[174] *Idem* at 790; in *Adams v Cape Industries Plc v Cape Industries plc* [1991] 1 ALL ER 929 (CA) at 1026 the court states that the separate legal personality of companies will still be maintained even when the initial set up of the company is aimed towards avoiding future legal liability which might rest on another company within the group.
[175] 1978 SLT 159.
[176] *Supra* note 172 at 1022.
[177] [1998] BCC 607.
[178] Farouk HI Cassim et al *Contemporary Company Law 2ed* (2012) at note 761.
[179] 1993 (2) SA 669 (A).
[180] *Supra* note 7 at 51.
[181] 1993 (2) SA 669 (A).

the one which was supposed to insure the subsidiary's property. The liquidator of the holding company rejected this argument, by counter-argument stating that directors of the holding company do not have any fiduciary duties towards the subsidiary company.[182]

4.4 Relaxed approach

In *DHN Food Distributors Ltd v London Borough of Tow Hamlets*,[183] DHN ran a wholesale cash and carry business. It ran its operations from the premises owned by Bronze, one of its wholly owned subsidiary companies. The directors and shareholders of DHN were the same as those of Bronze. The land on which the business was ran was acquired. DNH argued that it has a claim for compensation for disturbance even though the land was on the premises owned by its wholly owned subsidiary.

SHAW LJ argued that the facts of the matter will dictate whether a group of companies operate as one or whether they are single entities. In this case, the judge argues that the "identity and community of interest" of the group of companies should be taken into account. The main idea argued here is that the directors of DHN were at will to grant or take away the license which was given to bronze and that this ultimately results in an "indissoluble relationship."[184]

The court further argues that a group of companies can be considered as a single economic unit if it can be found that one holding company owns all the shares of the subsidiary company and can therefore "control every movement of the subsidiaries." It further argues that these subsidiaries are "bound hand and foot to the parent company and must do just what the parent company says."[185]

4.5 Agency relationship

In *Smith, Stone & Knight Ltd v Lord Mayor, Aldermen Citizens of the City of Birmingham*[186] the court held that in a group of companies, a principal-agent relationship can exist, with

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[182] *Supra* note 7 at 52.
[183] [1976] 3 ALL ER 462.
[184] *Idem* at 473.
[185] *Idem* at 467.
[186] [1939] 4 ALL ER 116.

the result that the subsidiary can be considered to be the agent of the principal.[187] It stated six factors which should be taken into account when determining whether a principal-agent relationship exists in a group of companies. These factors are as follows:

a) Were the profits treated as those of the holding company?

b) Were the persons conducting the business appointed by the holding company?

c) Was the holding company the head and brain of the trading venture?

d) Did the holding company govern the venture and decide what should be done and what capital should be embarked on the venture?

e) Were the profits made by the skill and direction of the holding company?

f) Was the holding company in effectual and constant control?[188]

In Adcock-Ingram Laboratories v SA Druggists Ltd; Adcock-Ingram Laboratories Ltd v Lennon Ltd[189] it was held that the agency principle is not factored only on the premise that there is control of the subsidiary company by the holding company simply because the directors of the holding company are the same as those of the subsidiary company.[190]

4.6 Conclusion

It is submitted that the relaxed approached should be followed, with the result that the holding company and subsidiary company will both maintain their separate legal personality. This submission does not come without qualification. It is applicable against attempts to treat the holding and subsidiary companies as single entities despite there not being any abuse of the separate legal personality of the subsidiary company. Where there is an abuse of the separate legal personality between group companies, such as in *Cape Pacific Ltd v Lubner controlling Investments,*[191] the corporate veil should be pierced.

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[187] *Supra* note 7 at 52.
[188] *Supra* note 7 at 53.
[189] 1983 (2) SA 350 (T) 353.
[190] *Supra* note 7 at 53.
[191] *Supra* note 24.

CHAPTER 5: COMPARISON WITH ENGLAND AND AUSTRALIAN LAW ON PIERCING OF THE CORPORATE VEIL

5.1 Introduction

In this chapter, England and Australian law on piercing the corporate veil will be analyzed, to discover whether their philosophy on this remedy can be useful in solving the challenges faced by the South African courts. A greater degree of the discussion will be placed on the approach which the English and Australian courts have taken when determining whether to pierce the corporate veil.

5.2 Approach

In *Adams v Cape Industries*[192] it was held that courts do not have a general discretion to pierce the corporate veil, even in instances where the courts find that it would be in the interests of justice to do so.[193] It holds that:

> "We do not think that the cases relied on go nearly so far as this. As [counsel for Cape] submitted, save in cases which turn on the wording of particular statutes or contracts, the court is not free to disregard the principle of *Salomon v Salomon v A Salomon v Salomon & Co Ltd* [1897] AC 22, [1895–9] All ER Rep 33 merely because it considers that justice so requires. Our law, for better or worse, recognizes the creation of subsidiary companies, which though in one sense 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."[194]

Lord Neuberger in *Prest v Petrodel Resources Limited*[195] provides an analysis on the approach which courts have followed or ought to follow. At first, the judge acknowledges

[192] [1991] 1 ALL ER 929 (CA).
[193] *Idem* at 1019.
[194] *Idem* at 995.
[195] [2013] 2 AC 415.

that in most cases "it is impossible to discern any coherent approach, applicable principles, or defined limitations to the doctrine."[196] The judge then goes further to note that "there is obvious value in seeking to decide whether the doctrine exists, and if so, to identify some coherent, practical and principled basis for it, if we can do so in this case."[197]

The judge supports the proposed approach brought forward by Lord Sumption, which requires that the veil should be pierced where actions by members of a company amount to an evasion of legal obligations or "whose enforcement he deliberately frustrates by interposing a company under his control."[198]

In *Woolfson v Strathclyde Regional Council*[199] it was held that piercing of the corporate should only be used in exceptional circumstances, particularly where the facts indicate "that it is a mere facade concealing the true facts."[200]

In *Trustor AB v Smallbone*[201] it was held that the veil will be pierced where the company was used as a "façade" or "sham" and where the abuse of the corporate structure of a company result in some form of impropriety.[202]

In *Sharrment Pty Ltd v Official Trustee in Bankruptcy*[203] a sham was described as follows:

> "A 'sham' is…something that is intended to be mistaken for something else or that is not really what it purports to be. It is a spurious imitation, a counterfeit, a disguise or a false front. It is not genuine or true, but something made in imitation of something else or made to appear to be something which it is not. It is something which is false or deceptive."[204]

[196] *Idem* at 64.
[197] *Idem* at 65.
[198] *Idem* at 81.
[199] 1978 SC(HL) 90.
[200] *Cape Pacific Ltd v Lubner controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 37-38.
[201] *Trustor AB v Smallbone (No 2)* [2001] 1 WLR 1177.
[202] *Idem* at 23; See also *Ben Hashem v Al Shayif* [2009] 1 FLR 115 at 159-164.
[203] *Sharrment Pty Ltd v Official Trustee in Bankruptcy* (1988) 82 ALR 530.
[204] *Idem* at 537; Ian M Ramsay & David B Noakes. 'Piercing the Corporate Veil in Australia' (2001) 19 *Company and Securities Law Journal* 250-271 at 13.

In *Dennis Willcox Pty Ltd v Federal Commissioner of Taxation*[205] it was held that creating or using a company in such a way that will amount to evading a legal obligation or fraud is sufficient to pierce the corporate veil.[206]

Flexible v Categorizing approach

Lady Hale *Prest v Petrodel Resources Limited* is critical of the evasion principle approach adopted by Lord Sumption and Lord Neuberger, particularly with respect to whether this categorizing approach covers all possible situations where piercing of the corporate veil can find application. Lady Hale holds as follows:

> "I am not sure whether it is possible to classify all of the cases in which the courts have been or should be prepared to disregard the separate legal personality of a company neatly into cases of either concealment or evasion. They may simply be examples of the principle that the individuals who operate limited companies should not be allowed to take unconscionable advantage of the people with whom they do business."[207]

Lord Mance also advices that it is "dangerous" to use a categorizing approach, which essentially amounts to foreclosing all future possible situations which may arise that may require piercing of the corporate veil.[208]

5.4 Remedy of last resort

In *Ben Hashem v Al Shayif*[209] it was held that piercing of the corporate veil should be used when other available remedies were not of assistance.[210] This view finds support from Lord Clarke.[211]

5.5 Conclusion

[205] *Dennis Willcox Pty Ltd v Federal Commissioner of Taxation* (1988) 79 ALR 267.
[206] *Idem* at 272.
[207] *Idem* at 92.
[208] *Idem* at 100.
[209] [2009] 1 FLR 115.
[210] *Supra* note 203 at 103.
[211] *Ibid*.

This chapter looked into the position of England and Australian law on piercing the corporate veil, with the aim of determining whether any principles that their courts have applied can serve as guidelines for the remedy of piercing of the corporate veil in South Africa.

Prest v Petrodel Resources Limited[212] provides an in-depth analysis of the position in England regarding piercing of the corporate veil. It is submitted that the evasion principle, as discussed in this case,[213] should be one of the grounds that are fully recognized for piercing the corporate veil.

The view by Lord Mance that applying a categorizing approach is "dangerous" is supported, on the grounds that future situations that justify piercing of the corporate veil may be excluded.[214] A flexible approach should therefore be followed.

The view in *Ben Hashem v Al Shayif*[215] that the corporate veil should only be pierced when other remedies are of no assistance,[216] is not supported in this dissertation. The submission is that the remedy should be available despite the existence of an alternative remedy.

[212] *Supra* note 195.
[213] *Supra* note 202.
[214] *Supra* note 204.
[215] *Supra* note 209.
[216] *Supra* note 206.

CHAPTER 6 CONCLUSION AND RECOMMENDATIONS

6.1 Introduction

This dissertation has considered the position of the law with respect to piercing of the corporate law in South Africa using qualitative research methods. A comparison was made with cases of piercing the corporate veil in England and Australia.

This chapter will fully set out the recommendations that are best suited to resolve the problem-statements that were laid out in chapter one.

6.2 Approach to piercing the corporate veil

6.2.1 Flexible approach versus categorizing approach

It is submitted that the flexible approach as laid out in *Cape Pacific Ltd v Lubner controlling Investments*[217] should be followed.[218] This requires that grounds for piercing the corporate veil should not be categorized, as was the approach in *Botha v Van Niekerk*.[219] This approach further requires that the facts of each case should be judged on their own merit.[220] The flexible approach is preferred, to avoid situations were cases fall outside of categories whilst on principle they would permit piercing of the corporate veil.[221]

One challenge which is brought about by the flexible approach is the inability to determine all circumstances upon which the remedy can find application. This challenge is important because it brings about uncertainty in the law regarding the application of the remedy. This will make it hard to rely on the remedy, as facts may dictate that the remedy is applicable, but the uncertainty or unawareness regarding the possible circumstances may limit the number of cases that rely on the remedy.

In considering the above stated challenge, courts should apply the principles laid down in previous cases, whilst avoiding a categorizing approach. In this regard; fraud, dishonesty

[217] *Supra* note 24.
[218] *Idem* at 37.
[219] *Ex Parte Gore* [2013] 2 All SA 437 (WCC) at footnote 36.
[220] *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 802.
[221] Farouk HI Cassim *et al Contemporary Company Law* 2ed (2012) at 45.

and improper conduct, as expressed in various cases,[222] should be grounds from which the courts can pierce the corporate veil.

It is admittedly difficult to define what constitutes dishonesty and improper conduct. These terms can be broadly defined, the courts should therefore give them clear definitions. In *Ex Parte Gore*,[223] for instance, the court holds that unconscionable abuse, as found in section 20(9) of the Act, is wide enough to encompass terms such as 'sham' and 'device'.[224] It is admittedly not clear what these terms mean.

It is submitted that the evasion principle, as laid out in *Prest v Petrodel Resources Limited*[225] should constitute a ground for piercing the corporate veil. This ground applies to situations were a director, shareholder or company in a group of companies avoids a legal obligation through abusing the separate legal personality of a company.

The balancing approach is a useful guiding tool that courts can use when determining whether to pierce the corporate veil. This approach requires that a comparative trade-off must be made between arguments supporting preserving the separate legal personality of a company against policy considerations in favour of piercing the corporate veil.[226]

The challenge with the balancing approach is that it does not outline all the possible policy considerations which should be considered that support piercing of the corporate veil. It furthermore does not assist in determining how the arguments for and against piercing of the corporate veil should be weighed. The courts, when applying the balancing approach, as per the common law remedy, should always keep in mind that they do not have a general discretion to pierce the corporate veil.[227] They should therefore ensure that they do not pierce the corporate veil sparingly,[228] as it is a drastic remedy.[229]

6.3 Interpretation of section 20(9) of the Act

[222] *Supra* note 24 at 35; see also *The Shipping Corporation of India Ltd v Evdomon Corporation and Another* 1994 (1) SA 550(A) at 566C-F.
[223] *Supra* note 17.
[224] *Ex Parte Gore* [2013] 2 All SA 437 (WCC) at 34.
[225] *Prest v Petrodel Resources Limited* [2013] 2 AC 415 at 81.
[226] *Supra* note 24 at 803.
[227] *Hulse-Reutter v Godde* 2001 (4) SA 136 (SCA) at 20.
[228] *Supra* note 212 at 55.
[229] *Idem* at 46.

6.3.1 Unconscionable abuse

In *Ex Parte Gore* it was held that unconscionable abuse is wide enough to cover words such as 'sham', 'stratum', 'device' and 'conceivably much more'.[230] It is admittedly unclear as to why this interpretation was given by the courts. Neither the Act nor the court in *Ex Parte Gore* provide a definition of what 'unconscionable' means. This is problematic because it appears that the legislator is not interested in circumventing all kinds of abuse of the separation legal personality of companies, only those which are 'unconscionable'.

Section 65 of the Close Corporations Act contains a similar provision to section 20(9). The Close Corporation Act does not refer to 'unconscionable abuse', rather 'gross abuse'. In *Ex Parte Gore*, it was held that 'gross abuse' is of a more drastic standard than 'unconscionable abuse'.[231] There is however no justification as to why this the case. In light, the court indirectly calls into question the interpretive value of court decisions that dealt with section 65 of the Close Corporation Act.

It is submitted that section 65 of the Close Corporation Act and section 20(9), on principle, are both aimed towards providing a remedy for instances where the separate legal personality of a juristic person is violated. The two sections are focused on the act and not the consequence of the abuse. Court decisions that dealt with section 65 of the Close Corporation Act can therefore be of interpretational value.

It is submitted that the factors laid down in *Airport Cold Storage (Pty) Ltd v Ebrahim*[232] can be of value when determining whether there was unconscionable abuse. The factors are as follows:

> "a) The close corporation had formed part of a conglomerate of associated family businesses that had been conducted with scant regard for the separate legal personalities of the entities concerned,
>
> b) The close corporation had not kept proper books of account,

[230] *Ex Parte Gore* [2013] 2 All SA 437 (WCC) at 34.
[231] *Ibid*.
[232] Supra note 152.

c) The close corporation had opened without having appointed an accounting officer,

d) The close corporation had voluntarily assumed a debt owing by the family business when it was incorporated and had acquired significant debts from the start of commencing business, which had amounted to reckless trading."[233]

6.4 Remedy of last resort

It is submitted that the remedy of piercing of the corporate veil should be available despite the availability of an alternative remedy. The relevance of an alternative remedy, as noted in *Cape Pacific v Lubner Controlling Investments*, should only find expression when policy considerations for piercing the corporate veil are taken into account.[234]

Section 20(9) of the Act does not expressly provide for this remedy to be used only as a last resort. In Ex Parte Gore, it was held that this is a concession, or rather intent from the legislator that the statutory remedy can be triggered whenever facts amounting to 'unconscionable abuse' of a company's separate legal personality arise.

A possible challenge that comes with piercing of the corporate veil and allowing it to be available despite the existence of an alternative remedy, is that it could be used sparingly such that it is undermined.[235] It is submitted that for as long as the remedy is not applied arbitrarily, but that sound principles are correctly applied whenever the remedy is sought, then it will not be undermined.

6.4 Common law and Section 20(9) of the Act

It is submitted that the position in *Gore* that section 20(9) does not replace common law piercing of the corporate should be followed. This submission is based on two reasons. Firstly, the provisions of the section, particularly with regards to what 'unconscionable

[233] *Supra* note 212 at 58.
[234] *Cape Pacific Ltd v Lubner controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 40.
[235] *Supra* note 212 at 55.

abuse’ means provide interpretational difficulties. The common law developments may be of interpretational value in this regard.

Secondly, the availability of the common law remedy as well as section 20(9) provide a wider application of instances when the courts may pierce the corporate veil. This view supports the flexible approach, as it will allow for other instances of piercing the corporate veil to exist should the courts decide to give ‘unconscionable abuse’ a restrictive interpretation.

WORD COUNT (13619).

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