

**THE DERIVATIVE ACTION AND A MEMBER'S AUTHORITY TO  
REPRESENT A CLOSE CORPORATION IN TERMS OF SECTION 54  
OF THE CLOSE CORPORATIONS ACT 69 OF 1984**

*Naidoo v Dube Tradeport Corp* 2022 3 SA 390 (SCA)

**OPSOMMING**

**Die afgeleide aksie en 'n lid se bevoegdheid om 'n beslote korporasie kragtens artikel 54 van die Wet op Beslote Korporasies 69 van 1984 te verteenwoordig**

In *Naidoo v Dube Tradeport Corp* 2022 3 SA 390 (SCA) moes die hof beslis oor 'n eksepsie wat aangeteken is teen 'n besonderhede van vordering waarin die tersydestelling van die verkoop en oordrag van onroerende eiendom deur 'n beslote korporasie (as verkoper) aan die koper geëis is. Die beslote korporasie is tydens die transaksie deur die korporasie se enigste lid verteenwoordig. Volgens die besonderhede van vordering was die lid van die korporasie nie gemagtig om die verkoopskontrak aan te gaan nie, omdat die lid slegs genomineer was om die ledebelang te hou namens die voordelige houër. Een van die aspekte waaroor die Hoogste Hof van Appèl moes beslis, was of die voordelige houër op grond van die gemeenregtelike afgeleide aksie (soos bevestig in *Foss v Harbottle* (1843) 2 Hare 461; 67 ER 189) 'n aksie namens die beslote korporasie teen die koper en die genomineerde houër van die ledebelang kon instel. Die lid se beweerde gebrek aan magtiging is deur die koper op grond van artikel 54 van die Wet op Beslote Korporasies 69 van 1984 ("die Wet") betwis. Die Hoogste Hof van Appèl het beslis dat die beginsels in *Foss* op beslote korporasies van toepassing is. Verder is beslis dat die koper, op grond van sy kennis van die dispuut tussen die genomineerde houër en die voordelige houër van die ledebelang, nie op artikel 54 kon steun nie. In hierdie bespreking word die hof se interpretasie van artikel 54 in die konteks van die interne en eksterne verhoudinge van 'n beslote korporasie beoordeel. Ek neem ook die regsverhouding tussen die beslote korporasie en die genomineerde houër en voordelige houër van 'n ledebelang in oënskou. Ek kritiseer die hof se verwysing en toepassing van die leerstuk van toegerekende kennis in die konteks van artikel 54 op grond van die bepalings in die Wet en regspraak wat beslis het dat die kennisleerstuk nie op gewone persoonlike of vorderingsregte van toepassing is nie.

**1 Introduction**

Even though no new close corporation can be incorporated and registered since the commencement of the Companies Act 71 of 2008 on 1 May 2011, close corporations remain significant and important participants in the South African economy. In *Naidoo v Dube Tradeport Corp* 2022 3 SA 390 (SCA), the Supreme Court of Appeal recently dealt with important aspects of the law of close corporations. In its judgment the court had to deal with an exception that was raised to the first and second appellants' particulars of claim issued in the High Court. In the particulars of claim it was alleged that the first appellant was the beneficial owner of the only member's interest in a close corporation, cited as the second appellant in the appeal. The member's interest was held by the second respondent, the only nominee and only member of the close corporation. Alternatively, it was alleged that first appellant was the beneficial owner of 50 per cent of the member's interest held by the second respondent as the sole member in the close corporation (see para 2 read with para 4). While the High

Court dismissed the exception, it was upheld on appeal (see para 1 read with para 37). The Supreme Court of Appeal held that the merits of the exception must be decided on the basis that the factual allegations contained in the particulars of claim must be accepted “unless they are manifestly false” (para 18). This note provides an analysis of how the legal relationship between a beneficial holder and a nominated holder of a member’s interest in a close corporation may possibly affect the external relations of a close corporation with third parties. I also provide a critical perspective on the court’s application of the doctrine of notice in respect of the interpretation of section 54 of the Close Corporations Act 69 of 1984 (“the Act”). Although it is true that the merits of an exception must be adjudicated by assuming that the factual allegations on which the particulars of claim are based is correct, I argue that the Supreme Court of Appeal failed to consider adequately whether the factual allegations contained in the particulars of claim are sustainable in law to constitute a cause of action. By upholding the appeal and dismissing the exception, the court accepted the factual possibility that a dispute between a member of a close corporation and an alleged beneficial owner of a member’s interest may strip a third party of the protection afforded by section 54 of the Act in dealing with the close corporation. Although it may be possible that a member’s interest in a close corporation may be held by a nominee on behalf of a beneficial owner, section 30(2) of the Act provides that a member’s interest cannot be held jointly. In dealing with the alternative argument, I argue that the court failed to consider fully the statutory restrictions and limitations in the Act pertaining to the holding of a member’s interest in a close corporation. The ruling of the Supreme Court of Appeal also has implications for the interpretation of other provisions in the Act, such as sections 46 and 54. In conclusion I argue that the court’s interpretation of section 54(2) on the facts of this case is problematic, as it conflates the distinction that must be drawn between the internal and external relations of close corporations, and that the court further failed strictly to uphold the separate juristic personality of a close corporation.

## 2 Facts

### 2.1 *Background and the parties to the dispute*

Odora Trading CC was the second appellant. Sivaraj Naidoo, the second respondent, was the only registered member of the second appellant (para 2). The first appellant, Sagadava Naidoo, was the brother of the second respondent and alleged beneficial owner of the member’s interest held by the second respondent as a nominee (para 2). On 18 December 2015, the first respondent, Dube Tradeport Corporation, bought and took transfer of immovable properties (“the properties”) from the second appellant in terms of a sale agreement concluded by the second respondent for and on behalf of the second appellant with the first respondent (para 5). As the dispute involved immovable properties, the Registrar of Deeds Pietermaritzburg was cited as the third respondent (para 3).

### 2.2 *Particulars of claim*

In the High Court, the first and second appellant instituted action proceedings against the first, second, and third respondents (para 1). The first appellant instituted the action in his personal, as well as a representative, capacity on behalf of the second appellant (para 2). Relief was sought in the form of an order declaring the sale and transfer of the properties null and void with a further order that

these properties be transferred back to the second appellant (para 1). It was further alleged that the second respondent held the entire member's interest in the second appellant as a nominee of the first appellant, or, alternatively, that the first appellant was entitled to 50 per cent of the membership interest held in the second appellant (para 2 read with para 4).

### *2.3 Alleged grounds for setting aside the sale and transfer of the properties*

It is the case for the first appellant that the sale and transfer of the properties owned by the second appellant were a repudiation of the agreement (or agreements) that existed between the first appellant and the second respondent (para 1). According to this agreement (or agreements), the second respondent is the sole registered member of the second appellant and held the member's interest as a nominee on behalf of the first appellant (para 2). The agreements on which the first appellant relied were allegedly concluded on 20 January 2001 and during 1998 (para 2 read with para 4).

### *2.4 20 January 2001 agreement*

Based on this agreement, certain assets would be owned in equal proportions by the first appellant and the second respondent (para 4). These assets included the first appellant's loan account and member's interest in the second appellant (para 4). In terms of this agreement, the properties and assets would have been transferred to and held by the first appellant and second respondent in their own names (para 4).

### *2.5 1998 agreement*

In terms of this agreement, the second respondent would hold certain assets as a nominee on behalf of the first appellant (para 5).

### *2.6 13 January 2014 litigation*

Prior to the dispute coming before the Supreme Court of Appeal, the first appellant instituted separate legal proceedings against the second respondent on 13 January 2014 (para 5). In these proceedings the first appellant sought relief in the form of a transfer of his member's interest in the second appellant by the second respondent (para 5). While this litigation was pending, the properties were sold on 18 December 2015 by the second appellant to the first respondent (para 5).

### *2.7 Exception to the particulars of claim*

The exception was based on two grounds. In the first instance, the exception was directed at the first appellant's *locus standi* to institute legal proceedings on behalf of the second appellant, based on the derivative action. The exception was based on the first appellant's lack of membership of the second appellant (para 7). Secondly, it was argued in the alternative (based on section 54 of the Act, which specifically provides that the second respondent as a member of the second appellant may bind the second appellant in transactions with third parties) that the sale and transfer of the properties cannot be disputed based on the second respondent's lack of authority (para 7).

### 3 Judgment of the High Court

#### 3.1 *Membership and the common-law derivative action*

The common-law derivative action applies to close corporations (para 8). Despite the last-mentioned finding, the first appellant was unable to institute legal proceedings on behalf of the second appellant because the first appellant was not a member of the second appellant and, as a consequence, the first appellant could also not rely on the statutory personal action in section 49, or the statutory derivative action in section 50 of the Act (para 8). The provisions of section 50 were irrelevant because the first appellant relied on the common-law derivative action (para 8).

#### 3.2 *Section 54 and the authority of a member*

Section 54 of the Act protects third parties “against the negative effects of the *ultra vires* doctrine and the doctrine of constructive notice” (para 9). The court found that because the second respondent entered the sale of the properties as the sole registered member of the second appellant, section 54 of the Act afforded the second respondent the necessary authority to sell and transfer the properties to the first respondent on behalf of the second appellant (para 9).

In relation to section 54, the High Court held that despite the fact that the first respondent knew of the dispute between the first appellant and the second respondent in relation to the ownership of the member’s interest in the second appellant, such knowledge was not enough to strip the first respondent of the protection afforded by section 54 (para 10). The High Court stated (as quoted by the Supreme Court of Appeal in para 27):

“... [I] cannot conclude that [Dube] knew, or reasonably ought to have known the truth of the membership arrangement between [Sagadava] and [Sivaraji]. [Dube Tradeport] was plainly aware that the two brothers were in dispute. That is clear from the incorporation of the dispute in the sale agreement as mechanism for the first respondent to escape from the sale agreement. Even so, does that mean that Dube TradePort knew of the truth, or reasonably should have done so? Surely they probably did not – that is why the escape clause was included in the sale agreement – just in case they were being misled. Had they known, or been capable of establishing the truth, they would almost certainly have done so. The sale agreement was, after all, no trifling matter.”

### 4 Judgment of the Supreme Court of Appeal

#### 4.1 *Approach to factual allegations*

The Supreme Court of Appeal strongly objected to the reasoning adopted by the High Court in relation to section 54 (para 28). The appeal court held that because the High Court was not sitting as a trial court, the High Court was not in a position to determine whether the first respondent had knowledge, or ought to have had knowledge, in relation to the dispute between the first appellant and the second respondent affecting the second respondent’s authority to represent the second appellant (para 28).

#### 4.2 *Knowledge*

During the exception proceedings it was, according to the Supreme Court of Appeal, sufficient for the appellants to allege that there was a dispute between the first appellant and the second respondent, which affected the sale agreement

between the second appellant and the first respondent (para 29). For purposes of exception proceedings, the allegations made in the particulars of claim must be accepted as true, unless manifestly false (para 18 read with para 28). The effect of this approach is that the allegation must be accepted as true that the first respondent must have known, or reasonably ought to have foreseen for purposes of section 54(2) of the Act, that the first appellant, and not the second respondent, was the actual member of the first respondent. The court based this finding on the doctrine of constructive notice (para 30). The Supreme Court of Appeal discussed the doctrine of constructive notice in the context of the acquisition of assets and stated that a person who acquires an asset while knowing that someone else has a vested prior personal right “may be held bound to give effect to that right” (*ibid*).

#### 4.3 *Derivative action*

The first respondent argued that the second appellant could not institute legal proceedings by itself or with the assistance of a person who is not a member (para 13). The Supreme Court of Appeal provided a brief overview of the origin and nature of the common-law derivative action (para 11). Unless the wrongdoers are in control of the company, individual shareholders do not have the right to institute legal proceedings on behalf of a company when the cause of action vests in the company (*ibid*). There is no express adoption of the rule in *Foss v Harbottle* (1843) 2 Hare 461 490–491 into South African law (*ibid*). In the context of company law, the common-law derivative action is abolished and replaced by section 165 of the Companies Act (para 21). Section 165 does not affect the application of the common-law derivative action in relation to close corporations (*ibid*). Accordingly, the common-law rights of a member of a close corporation remain intact (*ibid*). This includes the rights of “an actual, unregistered owner of a member’s interest, to bring a derivative action” (*ibid*). Even though the first appellant was an unregistered member, the court concluded that the first appellant was entitled to rely on the common-law derivative action (*ibid*).

#### 4.4 *Section 54*

The Supreme Court of Appeal explained that the purpose of section 54 of the Act was to protect *bona fide* third parties against “the negative effects of the ultra vires doctrine and the doctrine of constructive notice” (para 24). However, the court rejected the first respondent’s reliance on the authority of the second respondent in terms of section 54(1) to represent the second appellant in transactions with third parties (para 25). According to the court, the first respondent knew, or reasonably ought to have known, that the second respondent had no authority to bind the close corporation. In pending legal proceedings, the ownership of the member’s interest in the second appellant and the ownership of the properties sold is placed in dispute. The first respondent knew, or reasonably ought to have known, that the second respondent owned only 50 per cent of the member’s interest in the close corporation or, alternatively, held the entire member’s interest as a nominee of the first appellant.

## 5 Analysis

### 5.1 *Excepting to pleadings*

The Supreme Court of Appeal based much of its judgment on the first appellant’s allegation that he was the beneficial owner of the sole member’s

interest in the close corporation or, in the alternative, that he and the second respondent were the joint owners or co-owners of the member's interest in the second appellant (paras 2 and 4). In terms of Uniform Rule 23(1), exceptions can be raised against a pleading that is "vague and embarrassing, or lacks averments which are necessary to sustain an action or defence". Unless the factual allegations are manifestly untenable, these facts must be accepted as true (*AB Ventures v Siemens Ltd* 2011 4 SA 614 (SCA) para 2). However, this is only one side of the coin: A court must not only consider the factual allegations, but also whether the factual allegations as contained in pleadings constitute a cause of action sustainable in law in the context of the "factual matrix" pleaded (see *Harms Civil procedure in the superior courts* (October 2021) B23.3).

In the present case, there were substantive legal aspects relating to the membership of a close corporation that deserved further attention. The first aspect relates to the legal relationship between a beneficial owner and its nominee, and between the beneficial owner and the close corporation. The second relates to the joint ownership of a member's interest in terms of the Act as pleaded by the first appellant (para 4). I must point out that it is not the purpose of this analysis to evaluate critically the appeal court's approach to the exceptions raised against a particulars of claim, but to analyse some important points of law raised on the facts of this case. However, a more detailed assessment of the law applicable to the factual allegations made in the particulars of claim could have assisted the court in dealing with some of the exceptions raised.

## 5.2 *Derivative action*

### 5.2.1 Basic principles

The Supreme Court of Appeal made some noteworthy remarks in relation to the common-law derivative action, which deserve comment. A close corporation is a separate juristic personality (s 2(2) of the Act). One of the legal consequences of being a separate juristic personality is that when a wrong is committed against the juristic person, it is the juristic person that must institute legal proceedings against the wrongdoer (*Itzikowitz v Absa Bank Ltd* 2016 4 SA 432 (SCA) para 10). This is because the cause of action vests in the juristic person and not in its shareholders or members (*Gihwala v Grancy Property Ltd* [2016] 2 All SA 649 (SCA) paras 108 and 109). Also, this approach is aligned with the common-law principles in *Foss* and is known, among other things, as the proper plaintiff rule. The judgment in *Foss* contains the non-intervention rule (Cilliers & Benade *Corporate law* (2000) 296–297). In terms of the non-intervention rule, courts are reluctant to interfere with the internal relations of a company because the internal company matters are to be decided by majority vote to which the minority is bound (*Foss* 189). A court will interfere with decisions taken by the majority only when those decisions are unlawful (Cilliers & Benade 296).

### 5.2.2 Beneficial ownership and the application of the rules in *Foss* to close corporations

The finding of the Supreme Court of Appeal that "the common law rights of members of close corporations, including an actual, unregistered owner of a member's interest, to bring a derivative action, are still available" (para 21) deserves further scrutiny. A distinction must be drawn between the "ownership" rights of a beneficial "owner" and the membership rights to which a member is

entitled (see *Oakland Nominees (Pty) Ltd v Gelria Mining & Investment Co (Pty) Ltd* 1976 1 SA 441 (A) 453, where the court pointed out with regards to the concept of a beneficial ownership of shares that it is not “juristically speaking, wholly accurate; but it is a convenient and well-understood label”). Unless it is clearly the objective of the legislature, a statutory provision does not override or amend the common law (*Hlumisa Investment Holdings (RF) Ltd v Kirkinis* 2020 5 SA 419 (SCA) para 44). This makes it possible for the common-law derivative action in *Foss* to coexist with the statutory derivative action in section 50 of the Act (para 20). However, the *locus standi* of a person to rely on either the common-law derivative action or the statutory derivative action in section 50 of the Act depends on that person’s membership of the relevant close corporation. The membership requirements of a statutorily created juristic person are usually stipulated in the applicable statute read with the juristic person’s constitutive documents, where applicable. The membership requirements of a close corporation are defined in the Act (s 29 read with s 28 of the Act). I submit that, although the rule in *Foss* may still find application, it cannot override the statutory definition and requirements for membership. The availability of the common-law derivative action cannot change the requirements for membership stipulated in a statute in terms of which a separate juristic personality has been incorporated. In the context of a close corporation, a person becomes a member only when that person’s name is recorded in the founding statement (s 12 of the Act). A beneficial owner cannot rely on membership rights and remedies, because the name of such a beneficial owner of a member’s interest does not appear in the founding statement. A close corporation recognises only its members (see, in the context of company law, *Oakland Nominees* 453). In terms of the agreement between a beneficial owner and a nominee, a beneficial owner has the right to acquire membership rights by having his or her name entered in the founding statement of the close corporation as a member (see *Nayager v Venter* 53041/2016 [2017] ZAGPPHC 729 (20 November 2017) para 12). A nominee holder acts on the instructions of the beneficial owner (see also, in the context of company law, *Smyth v Investec Bank Ltd* 2018 1 SA 494 (SCA) para 43). Applying these legal principles to the facts before the court, the first appellant is not a member of the second appellant, and accordingly the first appellant does not have the standing to rely on the common-law derivative action. Relying on the common-law derivative action instead of the statutory derivative action does not allow a person to circumvent the specific legal requirements for membership of a close corporation. Further, the Supreme Court of Appeal did not cite or deal with any authority for its finding that a beneficial owner of a member’s interest can rely on the common-law derivative action despite not being a *member* (para 21). I submit that the first appellant did not have *locus standi* to institute derivative legal proceedings based on the common law on behalf of the second appellant. This is because the first appellant was not a member of the second appellant.

### 5.3 *Litigation: A direct and substantial legal interest*

The Supreme Court of Appeal held that despite the fact that the first appellant was possibly a beneficial owner of a member’s interest in the second appellant, the first appellant had the necessary *locus standi*. The court apparently arrived at this conclusion based on the first appellant’s reliance on the common-law derivative action instead of the statutory derivative action in section 50 of the Act (para 22). To have the necessary *locus standi*, a litigant must have a direct

and substantial legal interest in a matter subject to litigation (*Tulip Diamonds Fze v Minister of Justice and Constitutional Development* [2012] 4 All SA 401 (SCA) para 13; *Timasani (Pty) Ltd (in business rescue) v Afrimat Iron Ore (Pty) Ltd* [2021] 3 All SA 843 (SCA) para 15). In relation to the beneficial ownership of shares it was held in recent judgments by the same court that a beneficial owner does not have *locus standi* entitling him or her to rely on remedies available to registered shareholders. In *Smyth v Investec Bank* (SCA) para 55, the court held that “as long as the nominees” names remained in the register of members, the beneficial owners lacked a legal interest in the subject-matter of the litigation”. While the beneficial owners of shares do hold an economic interest in relation to the specific company in which the shares are held, the nominees of these beneficial owners are the holders of the legal interest in a company (see *Smyth v Investec Bank Ltd* 2016 4 SA 363 (GP) para 71). This implies that a beneficial owner cannot enforce any membership rights against a company, because these rights are held by the nominee, which makes the nominee the holder of a legal interest in the company.

I submit that the same applies to a beneficial owner of a member’s interest in a close corporation. The beneficial owner of a member’s interest does not hold a direct and substantial legal interest to be enforced against the corporation and accordingly will not have *locus standi*. The direct and substantial legal interest in the litigation before the Supreme Court of Appeal is held by the second appellant and not the first appellant. Further, the first appellant did not have any direct and substantial legal interest in the management of the second appellant. This was an interest held by the second respondent.

#### 5.4 *Internal and external relationships of close corporations*

##### 5.4.1 Purpose and function of section 54

A close corporation is a juristic person that must be represented by a natural person or natural persons. Third parties dealing with a juristic person often find it difficult to determine whether the person or persons representing the juristic person are duly authorised to bind such juristic person to agreements or transactions. Based on the *ultra vires* doctrine, a juristic person may avoid liability on the basis that a contract or transaction falls beyond the scope of the juristic personality’s capacity (for an overview of the *ultra vires* doctrine, see Cilliers & Benade 181–182). In the context of close corporations, section 54 is significant. Section 54(1) provides that “[s]ubject to the provisions of this section, any member of a corporation shall in relation to a person who is not a member and is dealing with the corporation, be an agent of the corporation”. Section 54 promotes legal certainty and commercial efficiency, because this section provides clarity on two important aspects relating to the representation of the close corporation to third parties (see Meskin & Kunst *Henochsberg on the Close Corporations Act* (Aug 2019) 154). In the first instance, the effect of the provision is that any *member* of a close corporation may represent the close corporation. Secondly, irrespective of whether the transaction falls beyond the close corporation’s scope of business, a close corporation will be bound to a transaction concluded by a member with a third party (see s 54(2) of the Act).

##### 5.4.2 Section 54 and the *bona fide* third party

Section 54 of the Act states that a member of a close corporation has the power to act as an agent of the close corporation to bind it to transactions with third

parties, irrespective of whether the transaction falls beyond the capacity of the close corporation. Section 54(1) must be read with section 54(2), which provides that a member will have the power to bind the close corporation, “unless the member so acting has in fact no power to act for the corporation in the particular matter and the person with whom he deals has, or ought reasonably to have, knowledge of the fact that the member has no such power”.

Section 54 of the Act prevents a close corporation from relying on the *ultra vires* doctrine to avoid liability in terms of a contract concluded by a member on behalf of the close corporation with a *bona fide* third party. For this reason, section 17 of the Act provides that the doctrine of constructive notice does not apply to close corporations. Section 17 of the Act specifically states that “[n]o person shall be deemed to have knowledge of any particulars merely because” the founding statement or any other document of the close corporation is lodged or is kept at a registered office of the close corporation.

For purposes of section 54(2), the Supreme Court of Appeal accepted that the first respondent had knowledge, or reasonably ought to have had knowledge, of the dispute that existed between the first appellant and the second respondent at the moment when the sale agreement of the properties was concluded, and accordingly the first respondent could not rely on section 54(1) (paras 26 and 29). This finding was based on the “escape clause” incorporated in the sale agreement for the benefit of the first respondent (para 26). The court equated the position of the first respondent to that of the purchaser of immovable property, based on the following passage in *Dhayanunth v Narain* 1983 1 SA 565 (N) 565:

“... [A purchaser who] has been apprised, prior to purchasing the property, of the existence of some right in the property vested in a third party in such a way as to make it incumbent upon him to enquire, before purchasing the property, precisely what that right comprised. If he does not do so, he cannot be heard ... to say he did not know the precise nature of the third party’s right. The imperfection of his knowledge is attributable to his own act wilfully shutting his eyes and failing to see what was perfectly obvious.”

The Supreme Court of Appeal rejected the reasoning of the High Court that the first respondent’s mere awareness of the dispute between the first appellant and the second respondent is not enough to strip a person in the first respondent’s position from the protection afforded by section 54 (paras 27 and 28). Despite the fact that the first respondent allegedly did not have knowledge of all the details relating to the nature and possible outcome of the dispute between the first appellant and second respondent, the appeal court concluded that the first respondent was not *bona fide* for purposes of section 54(2) of the Act (paras 32 and 33). The court attributed the “imperfection” of the first respondent’s knowledge in relation to the dispute between the first appellant and the second respondent, to the first respondent’s own failure to conduct further investigations into the matter (paras 27 and 28). I submit that the insertion of an “escape clause” into the sale agreement was only to protect the interests of the first respondent and cannot be construed as a failure to further investigate the dispute or to find that the first respondent knew of the facts of the matter.

I further submit that section 54 limits a third party’s duty to investigate the internal relations of a close corporation to the constitutive documents, such as the founding statement that is filed with the Companies and Intellectual Property Commission and/or is open to public inspection at the registered office of the close corporation. A third party’s legal duty to investigate cannot extend beyond

the constitutive documents of a juristic person. Following this line of reasoning, there was no evidence that the second respondent's authority was restricted in the second appellant's founding statement. Accordingly, I submit on the facts before the court that knowledge of the dispute between the first appellant and the second respondent was not sufficient to trigger the provisions of section 54(2), because the legal duty of the first respondent to investigate did not extend beyond the constitutive documents of the close corporation. Considering that the second respondent was the only member of the second appellant and held all the managerial powers and authority, it could not reasonably be argued that the first respondent could have reasonably suspected that there were limitations or restrictions on the second respondent to act as an agent of the second appellant. Importantly, the source of the second respondent's authority was the provisions of the Act and his mandate was accordingly not solely dependent on the instructions of the first appellant. Further, I submit that if the circumstances of the case before the Supreme Court of Appeal prompted the first respondent to conduct further investigations, a reasonable duty to investigate further could not have gone beyond the founding statement of the close corporation. Although the first appellant was (based on the contractual relationship between the first appellant and the second respondent) entitled to have the founding statement amended to reflect the first appellant as a member of the second appellant, the first appellant was not a member of the second appellant when the properties were sold and transferred to the first respondent.

#### 5.5 *Problematic reliance on Dhayanunth*

The legal problem with which the court was confronted in *Dhayanunth* materially differs from the facts before the Supreme Court of Appeal in *Naidoo*. In *Dhayanunth*, the court had to deal with a situation where a property in which a third party vested limited real rights in the form of a *habitatio* was sold to a purchaser. The court had to determine whether the third party acquired the immovable property subject to an unregistered right of *habitatio*. The court disposed of the matter based on the doctrine of notice. The doctrine of notice entails that, unless the immovable property is acquired with knowledge of the unregistered right of *habitatio*, a third party acquiring an immovable property that is subject to an unregistered right of *habitatio* will not be bound to such an unregistered right. Further, the doctrine of notice dealt with in *Dhayanunth* does not apply to rights of a "purely personal nature but only to rights *in personam ad rem acquirendam*" (*Vansa Vanadium SA Ltd v Registrar of Deeds* 1997 2 SA 784 (T) 796–797; also *Low Water Properties (Pty) Ltd v Wahloo Sand CC* 1999 1 SA 655 (SE) 663). This makes the reliance on, as well as the application of the legal principles in *Dhayanunth* to the present case problematic.

The Supreme Court of Appeal cited *Dhayanunth* as authority to dismiss the first respondent's argument that it did not have knowledge of all the facts relating to the dispute between the first appellant and the second respondent. I submit that, for purposes of the present case, *Dhayanunth* is irrelevant. A close corporation is a separate juristic personality. Accordingly, a member (including a beneficial owner of a membership interest) does not have a right in respect of the assets of the close corporation. Ownership of these assets vests in the close corporation only. Neither the second appellant nor the first respondent were party to or bound to the agreement or agreements between the first appellant and the second respondent. Further, the last-mentioned agreements did not create

rights *in personam ad rem acquirendam* (right to claim delivery), because the relevant immovable properties were owned by the second appellant and not by either the first appellant or second respondent, which renders the doctrine of notice inapplicable. I submit that the appeal court's reliance on *Dhayanunth* and the passage quoted by the court to substantiate the finding that the first respondent was "bound" to the arrangement between the first appellant and the second respondent despite the "imperfect" knowledge of the first respondent, was misplaced.

#### 5.6 *Prohibition against the joint holding of a member's interest*

Only qualifying persons may hold a membership interest in a close corporation (see the definition of a "member" in s 1 of the Act). A close corporation cannot have more than ten natural persons, each holding a member's interest (s 2(1) read with s 29(1) of the Act). No member's interest may be held jointly (s 30(2) of the Act). Considering the statutory provisions of section 30(2) of the Act, I submit that the exception to the factual allegation by the first appellant that he and the second respondent held the member's interest in the second appellant on a 50/50 basis, should have been upheld, because this allegation cannot be sustained on legal grounds, rendering the correctness of the factual allegation irrelevant. Unfortunately, the Supreme Court of Appeal did not discuss section 30(2) in relation to the alternative factual allegation made by the appellants in their particulars of claim.

#### 5.7 *Section 46(b)(iv)*

The first appellant did not provide his written consent for the properties to be sold to the first respondent. The Supreme Court of Appeal referred to section 46(b)(iv), in terms of which a member or members holding a member's interest of at least 75 per cent must provide written consent for the acquisition or disposal of immovable property owned by a close corporation. Again, this highlights the predicament in which a third party in the position of the first respondent may find him- or herself when contracting with a close corporation. When reading the founding statement of the second appellant at the time of conclusion of the sale agreement, it had only one member – the second respondent. Accordingly, only the second respondent's written consent was required to dispose of the immovable properties owned by the second appellant. Section 46(b)(iv) serves as protection for members of close corporations against a member disposing of immovable property belonging to the close corporation. I submit that the first appellant's written consent was not required to sell the properties on behalf of the second appellant to the first respondent because the first appellant was not a member.

## 6 Conclusion

In the present case the Supreme Court of Appeal had to deal with an exception raised to a particulars of claim issued by the first and second appellants. The facts of this case raise some important questions of law in relation to the beneficial ownership of a membership interest in a close corporation. This includes whether a beneficial owner can rely on the common-law derivative action, as well as to what extent a third party doing business with a close corporation has a duty to investigate the internal affairs and relationships within the close corporation to determine whether a member has the authority to conclude duly authorised contracts on behalf of the close corporation.

In the litigation before the High Court and the Supreme Court of Appeal, the first appellant acted both in a personal and representative capacity. In his representative capacity, the first appellant instituted a derivative action on behalf of the second appellant based on the common law. The problem with the first appellant's reliance on the derivative action is that the first appellant was not a party to the founding statement relating to the second appellant. Put differently, the first appellant was, for purposes of the Act, not a member of the close corporation. Despite being a beneficial owner of a member's interest in the second appellant, I submit that the first appellant did not have *locus standi* to rely on the common-law derivative action to institute legal proceedings on behalf of the second appellant because a beneficial owner does not enjoy membership rights. The derivative action, both in its common law and statutory forms, is a membership right. Further, the first appellant as a beneficial owner does not have a direct and substantial legal interest in the litigation before the court, despite having an economic interest in the matter.

To protect the public when dealing with a close corporation, section 54(1) states that a member is authorised to conclude contracts on behalf of a close corporation. Section 54(2) qualifies section 54(1) by stating that reliance cannot be placed on section 54(1) when the third party "has, or ought reasonably to have, knowledge of the fact that the member has no such power". I submit that when circumstances prompt a third party to investigate the power of a member to bind a close corporation to contracts, the duty to investigate cannot extend beyond the founding statement or undisputed facts actually known by the third party. As argued above, the doctrine of notice could not be relied on. Firstly, this doctrine does not apply to pure personal rights and, secondly, the first appellant did not have any rights in relation to the property sold to the first respondent.

It was contended for the first appellant that the second respondent did not have the authority to bind the second appellant to the contract of sale with the first respondent without a mandate from the first appellant. In this regard I must point out that the power of the second respondent to represent the close corporation originated from the Act and not from the mandate of the first appellant. The second respondent was an undisputed member of the second appellant when the transaction between the second appellant and the first respondent was concluded and, accordingly, he had the power to represent the close corporation. This is the position unless a member's power to represent the close corporation is restricted in the founding statement or an association agreement, and such restriction is known or reasonably ought to have been known by the third party. The first appellant was only a beneficial owner and thus could not have been a party to the founding statement or any association agreement, if applicable. I submit that the first appellant's only recourse was to rely on the contractual relationship between the second respondent and himself to claim to register as a member of the close corporation, after which the first appellant would be able to exercise his membership rights such as to institute a derivative action.

WJC SWART  
*Universiteit van Pretoria*