IN THE GAUTENG DIVISION OF THE HIGH COURT

PRETORIA, REPUBLIC OF SOUTH AFRICA 20/3/14

CASE NO: 27635/2010

In the matter between:

CORINTH TRADING (PTY) LIMITED

[in liquidation] Plaintiff

and

(1) REPORTABLE: ~~YES~~ / NO

(2) OF INTEREST TO OTHER JUDGES: ~~YES~~ / NO

19/03/14
DATE

SIGNATURE

RENEY VAN GREUNEN First Defendant

APPOLLO PALLOURIOS Second Defendant

JAMES HENRY WHEELER Third Defendant

JUDGMENT

Tuchten J:

1 The plaintiff company ("Corinth"), before its liquidation, functioned as a vehicle for a venture conducted by the three defendants. Now under the control of its liquidators, it sued the three defendants on the grounds that they had caused Corinth to trade recklessly. Although a number of factual allegations supporting the conclusion of

recklessness were pleaded, the case essentially is that the three defendants used company money to pay themselves salaries totalling some R740 000 when at least one creditor, Midlands Logistics, had not been paid any part of the sum of R608 603 owed by Corinth to Midlands Logistics. In addition, the plaintiff relies on the fact that when Corinth reached the limit of the financing which its banker was prepared to extend, the defendants caused revenue due to Corinth to be paid into the second defendant's bank account.

2 Although no indication of the source of the alleged obligation not to trade recklessly was pleaded, counsel for Corinth made it plain that Corinth was relying on s 424 of the Companies Act, 61 of 1973. Omitting presently irrelevant wording, s 424 provides as follows:

> **Liability of directors and others for fraudulent conduct of business**
>
> (1) When it appears, whether it be in a winding-up, judicial management or otherwise, that any business of the company was or is being carried on recklessly or with intent to defraud creditors of the company or creditors of any other D person or for any fraudulent purpose, the Court may, on the application of the Master, the liquidator, the judicial manager, any creditor or member or contributory of the company, declare that any person who was knowingly a party to the carrying on of the business in the manner aforesaid, shall be personally responsible, without any limitation of liability, for all

> or any of the debts or other liabilities of the company as the Court may direct.
> (2)(a) Where the Court makes any such declaration, it may give such further directions as it thinks proper for the purpose of giving effect to the declaration, ...

3 The remedy is a punitive one. A director can be held personally liable for liabilities of the company without proof of any causal link between his conduct and those liabilities. The onus is upon the party alleging recklessness to prove it and, in civil proceedings, to establish the necessary facts on a balance of probabilities.

4 Knowingly, in this context, means having knowledge of the facts from which the conclusion is properly to be drawn that the business of the company was or is being carried on recklessly; it does not entail knowledge of the legal consequences of those facts. It follows that knowingly does not necessarily mean consciousness of recklessness.

5 Being a party to the conduct of the company's business does not have to involve the taking of positive steps in the carrying on of the business; it may be enough to support or concur in the conduct of the business.

6 Recklessness does not connote mere negligence but at the very least gross negligence. A person can act recklessly if he acts in a manner which is grossly careless: ie does something which in fact involves a risk, whether the doer realises it or not; and the risk being such, having regard to all the circumstances, that the taking of that risk would be described as reckless. It includes an attitude or state of mind characterised by an entire failure to give consideration to the consequences of one's actions, in other words, an attitude of reckless disregard of such consequences. Risk-consciousness in the realm of recklessness does not amount to or include that foresight of the consequences ("gevolgsbewustheid") which is necessary for *dolus eventualis*. The concept of reckless disregard of the consequences pertains both to foreseen consequences and culpably unforeseen consequences.

7 The test for recklessness is objective insofar as the defendant's actions are measured against the standard of conduct of the notional reasonable person. It is subjective insofar as one has to postulate that notional being as belonging to the same group or class as the defendant, moving in the same spheres and having the same knowledge or means to knowledge.

8 In the application of the recklessness test to the evidence before it, a court should have regard, *inter alia*, to the scope of operations of the company, the role, functions and powers of the directors, the amount of the debts, the extent of the company's financial difficulties and the prospects, if any, of recovery. The extent of a director's duty of care and skill depends to a considerable degree on the nature of the company's business and on any particular obligations assumed by or assigned to him. His duties and qualifications are not equal to those of an auditor or accountant. He is not required to have special business acumen or expertise, or singular ability or intelligence, or even experience in the business of the company. He is nevertheless expected to exercise the care which can reasonably be expected of a person with his knowledge and experience. A director is not liable for mere errors of judgment. In respect of all duties that may properly be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly. He is entitled to accept and rely on the judgment, information and advice of the management, unless there are proper reasons for querying such. While a director exercising reasonable care would not accept information and advice blindly, he is not bound to examine entries in the company's books. His access to the particular information and the justification for relying upon the reports he receives from others, for example, might be relevant factors to take

into account. If a company continues to carry on business and to incur debts when, in the opinion of reasonable businessmen, standing in the shoes of the directors, there would be no reasonable prospect of the creditors receiving payment when due, it will in general be a proper inference that the business is being carried on recklessly.[1]

9 Corinth's business involved the export of ore, mined in Postmasburg, to a single buyer. The ore was bagged at Postmasburg, transported by road to the coast and loaded from the trucks on which it had come first into containers and then into vessels.

10 Corinth's summons was never served on the first defendant. The estate of the third defendant has been sequestrated. The issue before me was thus only the liability of the second defendant. The second defendant was the only witness who testified at the trial. Additional evidentiary material was provided by documents and by a record of what was said by the defendants at an enquiry under the insolvency legislation held into the affairs of Corinth after its liquidation.

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1 These propositions as to the nature of reckless trading are derived from *Philotex (Pty) Ltd and Others v Snyman and Others: Braitex (Pty) Ltd and Others v Snyman and Others* 1998 2 SA 138 SCA 142-144.

11 The three defendants became acquainted while serving as security contractors in Iraq. After their contracts in that zone came to an end, they found themselves back in South Africa, without jobs. They decided to go into the import/export business.

12 They identified an opportunity. There was a mine in the Postmasburg district which produced manganese. The ore contained iron as well as manganese. The mine was controlled by Webmin Trading Limited ("Webmin"). They identified a purchaser: Shivam Iron and Steel Limited ("Shivam"), of Kolkota, in India. They brought buyer and seller together. Shivam sent out a representative. The defendants took Shivam's representative to the mine at their own cost and put Shivam and Webmin's agent, Heriot Commodity and Trade Finance (Pty) Limited ("Heriot") together. In about February 2008, Shivam and Webmin, through Heriot, concluded a written agreement ("the sale agreement") in terms of which Webmin agreed to sell to Shivam a minimum of 60 000 and a maximum of 100 000 metric tons of ore per month.

13 Webmin had to deliver the ore to a bagging facility designated by Shivam at the mine in Postmasburg. The price of the ore was $2,94 per percentage of manganese content per dry metric ton FOT Postmasburg.

14 On 13 February 2008, Shivam and Corinth concluded a written agreement ("the transport agreement"). Corinth had to have the ore bagged and transported by road to containers to be loaded onto vessels procured by Shivam in Durban or Maputo. The price payable to Corinth by Shivam under the transport agreement was expressed in the transport agreement in three options, depending on the road route and port selected. The quantity of ore to be bagged and transported each month was a minimum of 15 000 and a maximum of 30 000 metric tons per month.

15 Under the sale agreement, the ore was required to contain certain percentages of manganese and iron respectively. Broadly stated, the more manganese and the less iron, the better. Webmin guaranteed the manganese and iron contents under the sale agreement. Corinth did not guarantee this under the transport agreement. Corinth's obligation was merely to bag the ore delivered to the bagging station, transport it to the port and load it into containers and load those containers onto the vessel provided.

16 If the minimum quantity of ore, ie 15 000 tons per month, was bagged and transported, Corinth could anticipate revenue of some R20 498 000 and expenditure of R20 110 100 per month. If the minimum quantity was exceeded, the net revenue inflow to Corinth

could reasonably be anticipated to be greater because increased quantities were likely to attract only proportionately increased costs.

17 Using the minimum quantity of 15 000 tons per month, the three defendants could and did, according to a spreadsheet produced by one of them (probably the first defendant but certainly not the second defendant), anticipate a monthly net inflow of revenue to Corinth of some R360 000 per month.

18 Although there were initial teething problems, by March 2008 the venture appeared to be proceeding well. The three defendants procured Corinth as a shelf company, changed its name to Corinth by special resolution and on 20 March 2008 held a meeting. It seems that although the three defendants had equal shareholdings, the first defendant was the only one with business experience. The second defendant had at one time been in the SA Defence Force, with the rank of corporal, and the third defendant had formerly been a policeman.

19 At the meeting the second and third defendants asked the first defendant to define their roles and portfolios in Corinth. The first defendant declared himself to be managing director, the second

defendant to be financial director and the third defendant to be operations director. This was accepted by the other two defendants.

20 While the second defendant impressed me as an honest witness, he appeared to be lacking in even a basic knowledge of commercial affairs. His capacity for inferential reasoning seemed very limited. Although designated financial director and appointed a director of Corinth, the second defendant's duties were nothing more than clerical. When the first defendant provided him with an invoice reflecting an indebtedness on the part of Corinth, the second defendant had to pay the creditor as per the invoice and then hand the invoice over to Corinth's appointed accountant. The accountant kept Corinth's books. In addition, the second defendant had to attend at the port (in each case, as it happened, Durban) and, when the ore arrived in 34 ton trucks, facilitate the loading of the ore into containers and onto the vessels for onward shipment. The evidence did not disclose the destination of the vessels.

21 The second defendant loyally carried out the duties entrusted to him. Corinth had no sources of financing until July 2008 except for what the defendants could raise in their personal names. Corinth's bank statements show that over and above payments to Corinth's creditors, only modest amounts were paid out by Corinth for travelling and

subsistence on the part of the second and third defendants, usually to Durban to facilitate the loading of the ore. The second defendant explained that on occasion he and the third defendant had spent the night in their vehicle at the quay in Durban to make sure that the ore was not stolen.

22 But although the progress of the manganese project was relatively slow, it appeared to be steady. In March 2008, Shivam established a letter of credit in favour of Corinth for $255 100 per month. The quality of the ore at the mine was tested at the instance of Shivam, which paid the fee for testing to Corinth during May 2008. On 26 May 2008, Corinth invoiced Shivam, in advance of shipment, for 1 065,95 tons of ore at $9,25 per ton plus $2 per ton for "project management".[2]

23 This shipment was in the nature of a trial run. All appearances were that the trial run was successful, because on 2 and 3 June 2008, Shivam paid into Corinth's account with Nedbank the sums of R962 029 and R91 136 respectively. Although there was no evidence of the rand dollar exchange rates, the likelihood is that the invoice of 26 May 2008 was paid in full. The evidence is that ore continued to arrive at the docks in Durban and that all the ore which arrived was loaded onto vessels for shipment in accordance with Shivam's

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2 Whether this $2 per ton was in fact for bagging was not explained in the evidence.

instructions. It was common cause that after the trial run of some 1 000 tons, another approximately 1 000 tons of ore was later shipped in accordance with Shivam's instructions.

24 The payment into Corinth's account of the two amounts I have mentioned meant that on 3 June 2008, Corinth had a credit balance with its banker of R1 052 486. The defendants used this money to pay Corinth's creditors, including themselves. On 3 June 2008 they paid themselves R150 000 each. On 17 June 2008, they paid themselves R80 000 each. This was the first money that any of the defendants had drawn from Corinth. They reflected the payments to themselves, in accordance with the advice of their accountant, as salaries.

25 Apparently on the strength of Corinth's prospects under the transport agreement, its only asset and only source of revenue, the first defendant managed to raise a short term loan of some R690 000 on overdraft with Corinth's banker. On 5 July 2008, this overdraft facility was used, together with the balance of the money received from Shivam, to pay Boswil Vervoer CC, a road transporter employed to carry ore to Durban, the sum R764 871.

26 Then Corinth hit a snag: it needed additional finance and its banker was not prepared without more to provide it. The first defendant told the second defendant that he was negotiating on the overdraft with the bank and asked the second defendant if he, the second defendant, would be prepared to "lend"[3] Corinth his personal bank account. The second defendant agreed immediately to do so. The second defendant appreciated that his bank account was needed because it was anticipated that further revenue would be forthcoming from Shivam, but that if this further revenue were at that stage paid into Corinth's bank account, it would go to pay off the overdraft and would thus not be available to Corinth.

27 On 13 August 2008, an amount of R347 063 was paid into the second defendant's personal bank account. The second defendant used nearly all of it to pay Corinth's creditors. At the time this money arrived, the second defendant's personal bank account was in overdraft to the sum of R15 962. He paid the first and third defendants R30 000 each. He paid his own parents R1 000. He paid two additional amounts of R10 000 to each of the first and third defendants. The remaining few thousand rands, apart from two lottery payments totalling R439, went towards the second defendant's modest living expenses.

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3 The term used in the evidence was "borrow".

28 It seems that Corinth in all employed three road transport contractors. The first, as I have mentioned, was Boswil Vervoer. The second was apparently Kritzinger Transport. The third was Midlands Logistics. Midlands Logistics did transport work for Corinth to the extent of R608 603. All of this was due by 15 July 2008. No part of it was paid.

29 A final payment of R80 083 was made into Corinth's bank account on 4 August 2008. I have mentioned that a second shipment totalling in the region of 1 000 tons went off. It seems that Shivam did not pay the full amount due to Corinth in respect of this shipment. Judging by what was paid in respect of the first shipment, something in the order of R1 million was due by Shivam to Corinth in respect of the second shipment. But Shivam only paid Corinth, in respect of the second shipment, the sums of R347 063 and R80 083. There was nothing in the transport agreement that entitled Shivam to withhold payment to *Corinth* on the ground of deficiencies in the quantity or quality of the ore. So Corinth, and the defendants, were entitled to assume that Corinth was due a further about R600 000, all of which would become available to pay Corinth's creditors and the defendants themselves.

30 But then the venture collapsed. By notice of motion lodged with the registrar on 25 August 2008, Midlands Logistics applied to this court under case no. 40110/2008 to wind up Corinth on the ground that

Corinth was unable to pay its debts. Corinth gave notice of intention to oppose but did not thereafter deliver any affidavits and on 18 September 2008 a provisional winding-up order issued and was made final on 21 October 2008.

31 The reason why Corinth became unable to pay its debts was, quite simply, because Shivam withdrew (to use a neutral term) from its contracts with Webmin and Corinth. The only evidence before me explaining why Shivam so withdrew is a letter from Khaitan & Co, Shivam's Kolkota advocate and solicitor, dated 19 September 2008. The suggestion in this letter is that Webmin was unable to supply either the minimum quantities of ore promised or the quality of manganese ore promised. There is no suggestion that Corinth was at fault in any way.

32 There is no evidence to suggest that Shivam had warned that it was contemplating withdrawing from the sale and transport agreements or that the quality of the ore was in issue. The only evidence which suggests that there was ever a problem with the ore supply is contained in the letter of Khaitan &Co. The suggestion in that letter is that on 4 July 2008 Shivam complained to Heriot that Heriot (sic) was committed to supply 1 500 tons of ore a week but had only supplied

200 tons and that on 15 July 2008, the first defendant wrote to Heriot with a similar complaint.

33 When the salary payments of June 2008 were made, the second defendant had no reason to believe that these payments might compromise Corinth's ability to pay its creditors. The initial teething problems appeared at that point to have been resolved with Shivam's payment in full for the first some 1 000 ton shipment. The use of the second defendant's bank account is of the same order. The second defendant had every reason to believe that Corinth's financial difficulties were merely due to a delay in payment of the balance owed for the second shipment and that once Webmin began to deliver in the promised quantities, Corinth would prosper. There is no reason to believe that the second defendant came into any information after the payment of the R347 063 into his account that might have warned him of Shivam's imminent withdrawal from the agreements.

34 In my view Corinth has an additional difficulty: the defendants had drawn no money at all during the five months preceding June 2008. By June 2008, they had reached the end of their financial resources. The second defendant testified that he had gone into debt to fund his participation in Corinth's business. The likelihood is that the other directors had similarly incurred debts. The business of Corinth could

not continue unless the defendants received something during June 2008 out of the money received by Corinth. So the submission of counsel for Corinth, that the defendants ought not to have paid themselves anything at all, cannot be correct. The question then arises: how much ought the defendants to have paid themselves in the period June to August 2008? There is no evidential material before me upon which to answer that question. The onus in this regard rests on Corinth. The absence of evidence therefore operates against Corinth.

35 And then, on the probablilities, both Nedbank and Midlands Logistics risked dealing with Corinth on the strength of the same information which was available to the defendants collectively. There is no suggestion in the pleadings, the evidence or in the record of the enquiry and the insolvency legislation that either of these creditors was misled as to Corinth's prospects. If the risks incurred by these creditors were acceptable to them as reasonable men of business, there is no reason why they should not have been aceptable to the second defendant.

36 And finally, the payments by the defendants to themselves had no impact on the ability of Corinth to carry on business. This is not a case of the directors of a business depleting its cash reserves and thus

causing the business to fail. Corinth's business failed because Shivam withdrew from the sale and transport agreements. It may be (I express no opinion on the point) that some of the payments made by Corinth constituted preferences. But the mere conferring of preferences does not necessarily, and in the present circumstances did not, assuming preferences, constitute recklessness.

37 I therefore conclude that Corinth has failed to prove that the second defendant conducted the business of Corinth recklessly. This is a commercial dispute. Costs must follow the result.

38 I make the following order: The plaintiff's claims against the second defendant are dismissed with costs.

NB Tuchten
Judge of the High Court
19 March 2014