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112/92

Case No 417/90

IN THE SUPREME COURT OF SOUTH AFRICA

APPELLATE DIVISION

In the matter between:

JOHN ALBERT HULETT	First Appellant
PAULA TOWNSEND	Second Appellant
ANGELA FOWLDS (born TOWNSEND)	Third Appellant
SALLY MAINGARD (BORN TOWNSEND)	Fourth Appellant

and

BRETT HULETT	Respondent

CORAM: HOEXTER, VAN HEERDEN, NESTADT, MILNE JJA et NICHOLAS, AJA

HEARD: 5 May 1992

DELIVERED: 2 JUNE 1992

J U D G M E N T

HOEXTER, JA .....

HOEXTER, JA

In terms of a written agreement of sale concluded at Durban on 10 March 1988 ("the contract") the four appellants sold certain shares and loan accounts in Stanger Quarries (Pty) Ltd ("the company") to the Brett Hulett Family Trust ("the trust") for R700 000. The respondent is the trustee of and a beneficiary under the trust. The appellants allege that they were induced to enter into the contract by the fraudulent deception of the respondent. Electing to abide by the contract the appellants instituted an action for damages for fraud against the respondent in the Natal Provincial Division. The respondent defended the action.

The trial was heard by Thirion J. The trial judge ordered absolution from the instance with costs. The costs awarded included the costs of two counsel as well as those occasioned by an adjournment of the trial on

18 April 1989. With leave of the trial judge the appellants appeal to this court against the whole of the judgment of the court below.

The essential facts in the case are hardly in dispute. From the sorry tale of events unfolded by the evidence there emerged the following three main characters:-

(1) The first appellant: Mr J A Hulett, who was the first plaintiff in the action. In this judgment reference will be made to him as "JH".

(2) The respondent: Mr B Hulett. For convenience I shall refer to him as "the defendant."

(3) Mr D B Townsend ("Townsend"). The second, third and fourth appellants, who were the second to fourth plaintiffs in the action, are the daughters of Townsend.

JH, the defendant and Townsend are farmers on

the Natal North Coast. All three started farming in the same area at about the same time. JH and Townsend were among the witnesses called at the trial. From their evidence it is clear that between the three very close ties had existed since their schooldays. They took part in sport together. Their respective families lived on intimate social terms. The families shared their vacations, and they also travelled overseas together. JH's wife is a godmother to the defendant's daughter; and the defendant and his wife are godparents to JH's son. JH and the defendant are second cousins. Townsend is not related to them by blood, but in his evidence JH said that:-

> "Townsend's family and our families were very, very close."

Townsend testified in the same vein. He said that they "all socialised together"; and he gave the following description of his relationship with the defendant:-

> "The Defendant and I have been .... best friends for the last forty odd years. We have been on holiday together, we had houses at the beach together, alongside each other, the Defendant proposed a toast at my eldest daughter's wedding ...."

In what follows, collective reference to JH, Townsend and the defendant will, for the sake of brevity, be made as "the trio"; and to the second, third and fourth appellants as "the daughters."

In the Stanger district of Natal there is a farm called "Sondela" ("the farm") which is owned by the Sondela Sugar Company (Pty) Ltd ("the SSC"). The shares in the SSC are held by the trust. At the beginning of 1984 a company ("Casrob") held a mining lease over 25 ha of the farm on which there was a disused quarry. Casrob, which was controlled by a Mr Mike Roberts ("Roberts"), had quarrying machinery for sale at a price of R500 000. With a view to the further exploitation of the quarry the defendant during May/June 1984 approached

JH and Townsend. The defendant suggested that they should get together a consortium of 15 to 20 people to raise R500 000 in order to finance a company which would take over the mining lease and run the quarry. To this suggestion JH responded by saying that he -

> "....wasn't interested in going into partnership with 15 or 20 people."

and he made a proposal, with which Townsend agreed, that participants should be limited to 4 or 5 persons. The upshot was that on 31 July 1984 the company was registered with an issued share capital of 150 shares. It had the following five directors: JH, Townsend, the defendant, Roberts and one Mr Dick Jones ("Jones"). JH was the first chairman of the board of directors. Thirty shares were registered in the name of each director except Townsend. The remaining 30 shares were divided equally between the daughters; but thereafter Townsend himself acted for and on behalf of the daughters in all matters

and negotiations affecting the shares thus registered in the names of the daughters.

The company arranged for a bank overdraft with a limit of R150 000, and as security therefor each director signed a personal guarantee for R30 000 in favour of the bank. Save for Roberts each director lent the company R100 000, such loans being reflected as loan accounts in the books of the company. In lieu of a loan by him to the company Roberts reduced the price of the quarry machinery, which was sold by Casrob to the company, from R500 000 to R400 000. The quarry produced road and concrete stone which was sold commercially. Casrob ceded to the company its rights under the mining lease in respect of the aforesaid 25 ha ("the quarry land") of the farm. In terms of the lease the company thereafter paid to the SSC a royalty of 5% on the sale of quarry products. The SSC granted the company an option, which had to be

exercised by 31 August 1987, to buy the quarry land for R350 000 ("the option"). Jones was put in charge of the day to day running of the company.

By November 1984 the company was short of cash. It had to increase its overdraft limit to R300 000, and further personal guarantees were required by the bank. These were furnished by each of the directors save Jones. At the same time the company issued 15 additional shares. Of this further issue 12 shares were divided equally between JH, the trust and Roberts, and 3 shares were divided equally between the daughters. Initially the company operated at a loss. In March 1985 Mr R McLelland ("McLelland") was engaged as quarry manager, whereafter its operations began to show profits. In September 1986 McLelland lent the company R25 000, in return for which 18 shares in the company were issued to him. At the same time Jones decided to sever his association with the

company. His shares and loan account were bought by the remaining shareholders for R140 000.

The defendant visited the farm daily. Throughout he displayed great interest in the quarry; and he involved himself in its day to day running. In September 1986 the defendant succeeded JH as the chairman of the company. From time to time a matter informally discussed by the company's directors was the possibility of the sale of their shares should a purchaser "with the right price" approach them. From these discussions JH and Townsend gained the impression that it was the defendant's wish to retain some sort of interest in the quarry.

In or about May 1987 the defendant told JH and Townsend that a quarry company named Blue Circle Materials (Pty) Ltd ("BCM") was showing interest in the acquisition of the quarry. The defendant undertook to report back to

them if anything should come of it. During July 1987 the defendant telephoned JH to say that Roberts wished to sell his shares and loan account in the company for R150 000. The members of the trio were minded to buy out Roberts in equal shares. At the suggestion of JH, and in order to inform Roberts of the interest in the company shown by BCM, a meeting between the trio and Roberts was arranged. Having been duly apprised at the meeting that BCM's interest had been aroused, Roberts told the trio that he was content to accept the figure of R150 000. The minutes of a meeting of the directors held on 7 July 1987 record, **inter alia**, the acceptance by the trio of the offer by Roberts to sell his shares and loan account for R150 000; and a resolution that the company would exercise the option to purchase the quarry land from the SSC. In regard to the latter it was agreed that the defendant "was to approach Barclays Bank re finance."

Shortly thereafter the defendant had an interview with the manager of the Stanger Branch of the First National Branch during which he requested a loan of R375 000 in order to finance the purchase by the company of the quarry land. The request was refused.

In October/November 1987 the defendant reported to JH and Townsend that BCM had evinced further interest in the company; and that he would meet with the directors of BCM in this connection. The meeting having taken place, the defendant reported to JH that BCM had made an offer of R1,5 million for all the shares in the company and the loan accounts of the trio. The defendant went on to tell JH: (1) that this offer was far too low, and that he had declined it; (2) that the practical implication of this offer for JH was that his shares and loan account "would only be worth about R200 000"; and (3) that if JH were prepared to accept R200 000 for his shares and

loan account, he (the defendant) would buy out JH at such figure. JH refused this offer by the defendant.

Between 1 to 25 January 1988 JH was overseas. Prior to his departure he discussed with Townsend the possible sale of his shares. Townsend told him that the defendant had offered each of them R270 000. JH replied that he was not interested in selling at that price, but that he would accept R450 000 for his shares and loan account.

Mr B P Chaplin ("Chaplin"), who practises as a chartered accountant at Umhlali, was also a witness at the trial. Until October 1986 he had been the company's accountant. He was JH's accountant and he held his power of attorney. During the absence of JH overseas the defendant went to see Chaplin at the latter's office. The defendant mentioned that he planned to expand operations at the quarry, but that he was experiencing difficulty "in

motivating his partners to accept the idea." He told Chaplin that he loved the business of the quarry, and that it was his whole life. The defendant explained that he had come to see Chaplin with a view to securing control of the quarry, and he offered to buy out JH for R200 000. Chaplin pointed out that JH was overseas, and undertook to refer the matter to Townsend.

Chaplin had been succeeded as the company's accountant by Mr C J Galloway ("Galloway"). On 11 January 1988 a meeting took place at the defendant's home between the defendant, Townsend, McLelland and Galloway. According to Townsend he was told at the meeting that the company should spend R750 000 in the purchase of new equipment and in repair work. Townsend demurred. He took his stand on an earlier resolution of the company's board to the effect that large expenditure should be made only on the strength of signed contracts; and he pointed out

that JH was still overseas. To this the defendant reacted by saying that if Townsend and JH were not prepared to spend money on the quarry they should sell their shares to him for R200 000. Townsend reminded him that JH and Townsend had already turned down the defendant's earlier offer to buy them each out at R270 000.

A further witness at the trial was Mr E A Todd ("Todd"). He described himself as the managing director of Bay Stone Sales ("Bay Stone"), a partnership between two large companies, one of which was Murray and Roberts ("M & R"). Unbeknown to Townsend and JH, Bay Stone was interested in acquiring the company. The chairman of Bay Stone instructed Todd to "investigate Stanger Quarries". On 19 January 1988 Todd proceeded to the farm where he met the defendant at the quarry. Todd was shown round the quarry by the defendant and McLelland, who gave him details of the company's business activities and

assets. In discussions between the defendant and Todd mention was made of a possible sale which Todd considered to be "in the offing". Todd's visit to the quarry took place in the morning. During the afternoon of the same day Townsend went to the Umhlali Country Club in order to play golf with the defendant. There the defendant introduced him to Todd. Before the introduction Townsend and Todd were known to each other only by name. Townsend knew that Todd was "manager of Bay Stone Quarry". Todd knew that Townsend had a 30% shareholding in the company. Todd testified specifically that at their meeting he discussed with Townsend neither the company's quarry business nor the possible sale of the quarry to Bay Stone. When Todd was asked why he had avoided mention of these matters to Townsend, Todd displayed a measure of diffidence. His reply was:-

"I seem to recall Mr Brett Hulett indicating that it would not be necessary to discuss it..."

After JH had returned from overseas he and Townsend paid a visit to the offices of BCM on 1 February 1988. There they had discussions with two of BCM's directors, Mr E Leo ("Leo") and Mr W Hooper ("Hooper"). Leo told them that the offer previously made by him to the defendant had involved R427 000 for 30% of the Company's shares plus a loan account (i e a total of R1,281 million for the shares and loan accounts of the trio); and that this offer still stood. Before 1 February the defendant had told JH that, according to his information, if it bought out the company BCM would require for its operations not merely the quarry land but an extra area of the farm ("the extra land") in addition thereto. During the visit JH inquired of Leo whether this was in fact so. Leo replied that BCM regarded the acquisition of the extra land as desirable, but not absolutely necessary. Leo

said that he would be prepared to offer the defendant R14 000 per hectare for such additional land.

JH and Townsend promptly reported to the defendant what Leo had told them. The defendant appeared to be unmoved thereby, and he said that "there must be some mistake." This reaction on the part of the defendant caused JH and Townsend to visit BCM on the next day to obtain from Leo an informal written note setting forth the essence of what he had said on 1 February 1988. The note indicated that half of the R427 000 which Leo was prepared to offer each member of the trio would be paid in November 1988 and the balance (which would carry interest at the prime bank rate) would be paid in February 1989.

In connection with the company's exercise of the option JH and Townsend had undertaken to furnish guarantees to the SSC to secure two-thirds of the purchase price of R350 000. Such guarantees had to be lodged by 3

February 1988, but before that date the defendant had intimated orally to JH and Townsend that the period for lodgment would be extended by a fortnight. The company's attorney was Mr A M Brokensha ("Brokensha"), the senior partner of a firm of attorneys in Pietermaritzburg. Brokensha advised JH to secure written confirmation of the promised extension. Accordingly on 2 February 1988 JH drafted a short formal letter to this effect, addressed to Townsend and JH, for signature by the defendant on behalf of the SSC. The letter was delivered to the defendant's home on the same day. On the following day (3 February) the defendant arrived at JH's farm office early in the morning. According to JH the defendant -

> "....appeared to be very upset that we had asked him to sign this letter .... and said to us that we were great friends and we shouldn't have to ask him to put it in writing because his word was his bond ...."

JH told the defendant to calm down and gave him a cup of

tea. For the ensuing half-hour they discussed the future of the company. The defendant said that what Roberts had been paid out represented a fair price, and he urged JH to accept the same price (R150 000) for his interest in the company. The defendant went on to say that he had always been very interested in the quarry; that he wanted a controlling share; and that if JH sold his shares to the defendant the latter would acquire a controlling interest. JH turned down the offer so made, and he pointed out that a further meeting with the directors of BCM would shortly take place.

Such a meeting was in fact held in Chaplin's office on Monday 8 February 1988. It was attended by Leo, Hooper, Townsend, JH and Chaplin. Before the meeting the defendant had again indicated to JH and Townsend his belief that should BCM decide to acquire the company it would insist upon the purchase by it of the

extra land. On this point JH and Townsend sought clarity at the meeting. Once again Leo's attitude was that while BCN would prefer to acquire the extra land, this was not essential. JH and Townsend further inquired of Leo whether he was prepared to buy a 60% shareholding (the shares held by JH and the daughters). Leo answered that he would be interested but that he would prefer 100%. JH and Townsend were asked by Leo to inquire of McLelland whether he would be interested in disposing of his 10% shareholding in the company for a consideration of R104 000. Two days later, on 10 February 1988, JH and Townsend met with McLelland and conveyed to him what Leo had said. McLelland responded by stating that he felt that his shares were worth more than R104 000; and that he was not interested in selling at that figure.

The defendant was a client of the Stanger branch ("the branch") of the First National Bank ("the bank").

On various occasions the defendant visited the branch in connection with the company and in quest of loans from the bank. During 1987/1988 the senior manager at the branch was Mr D L M Ducray ("Ducray"). The defendant's requests for financial assistance were made to Ducray and in regard thereto it was part of Ducray's duties to prepare and sign typewritten reports for consideration by the bank's General Manager ("the GM") at the bank's Natal head office in Durban. Such reports embodied both an account of what the defendant had said to Ducray and the latter's recommendations to the GM. Ducray was a witness at the trial. His testimony related to his interviews with the defendant as reflected in various head office advice forms prepared by Ducray to the GM. The relevant advice forms formed part of the documentary evidence before the court a quo, and their correctness was confirmed by Ducray.

On the same day that JH and Townsend explained

to McLelland what BCM offered for his shares, the defendant paid a visit to the branch in order to discuss with Ducray various alternative courses of action which the defendant was then contemplating. He told Ducray that BCM had made "a tentative offer" to buy the company for R1,5 million, and that he was trying to negotiate a better price. The advice form submitted by Ducray to the GM on 10 February 1988 reflects, **inter alia**, the following:-

> "Mr Hulett [i e the defendant] has still not made up his mind as to which direction he is to proceed i e:-
>
> 1) Sell the property [the quarry land] to the company for R350 000 as agreed.
> 2) Sell the property [the quarry land] and the surrounds [the extra land] for R775 000 to the company (refused by Co-director).
> 3) Buy out his partners for R500 000 to maximize his taking from any sale.
> 4) Sell to Blue Circle at offer price.
> 5) Negotiate a better selling price with Blue Circle.
> 6) Establish a Premix Plant on the site before selling at an increased price.

CONCLUSION

Mr Hulett is not a business entrepeneur and is being greedy regarding the value of the Quarry he owns. He is himself over extended and would do well to negotiate an outright sale with Blue Circle."

Two days later the defendant again visited the branch. Ducray's advice form to the GM dated 12 February 1988 stated, inter alia:-

"Hulett's Co-Directors have negotiated a deal for the sale of the company at R1,4 million to Blue Circle. The Shareholders will receive R220 000 immediately and R227 000 plus interest at prime rates in a year's time. The deal is conditional on the transfer of the quarry and surrounds into the name of the company. Blue Circle are willing to match the offer of R350 000 for the quarry and pay R140 000 for the additional 8,5 Ha.

.....

He is negotiating a deal (behind his Co-Directors backs) to sell the company and land to Murray & Roberts for R2 Million.

He wishes to better the present offer to his partners and intends to offer them R250 000 each cash plus a further R250 000 plus interest in a year's time.

> He requires us to grant bridging facilities of R500 000 to complete the first leg of the transaction but will only repay in a year's time. He does not wish Murray & Roberts to make their settlement immediately so that it will not become obvious to his Co-Directors that he has been unethical."

On 18 February 1988 Ducray sent to the GM a telefax reflecting the latest developments in the defendant's negotiations with M & R. The following are relevant extracts from the telefax:-

> "FURTHER TO MEMO 10TH AND 12TH FEBRUARY. MR HULETT STATES MURRAY AND ROBERTS MADE OFFER OF R2 MILLION WHICH IS TO BE CONFIRMED BY THEIR BOARD 3RD MARCH. .....
> REQUIRES TO MAKE IMMEDIATE OFFER R350 000 EACH TO CO-DIRECTORS AND R200 000 EACH IN A YEARS TIME. REQUIREMENTS THEREFORE NOW R700 000 BRIDGING FINANCE .....
> ARGUES THAT:
> 1) CONSIDERS HIMSELF TO BE WORTH R6/R7 MILLION - BALANCE SHEETS SHOW R3,4 MILLION OUR M/E R1 M.
> 2) STATES THAT IF MURRAY AND ROBERTS DEAL FALLS THROUGH HAS
> A) BLUE CIRCLE OFFER TO FALL BACK ON.
> B) WORST POSSIBLE POSITION COULD CONTINUE HIMSELF WITH QUARRY.

COMMENTS

.....

(C) COULD NOT CONTINUE WITH QUARRY WITHOUT FURTHER FINANCE."

On 29 February 1988 and at Chaplin's office there took place a meeting between Leo, Hooper, JH, Townsend and the defendant. There Leo and Hooper produced Heads of Agreement ("the BCM H/A"). Paragraph 7 of the BCM H/A read as follows:-

> "BCM offers to each of B Hulett, J A Hulett and D B Townsend the sum of R427 000 for their respective 30% shareholding in Stanger Quarries (Proprietary) Limited (SQ) and to R McLelland R104 000 for his 10% shareholding."

The BCM H/A provided that BCM would pay half of the consideration upon signature of the requisite transfer documents and the balance on 28 February 1989; and that interest on the balance would accrue at prime bank overdraft rate. A further term was that the company and the defendant would enter into an agreement permitting the company to extract stone from the quarry land "extended by

a further 10 hectares" in perpetuity for a royalty of 5% sales.

Immediately after the BCM H/A had been presented the defendant asked Leo whether or not BCM required the extra land measuring 10 ha. Somewhat to the surprise of JH and Townsend, Leo replied in the affirmative; and he offered to buy the extra land, which was planted to sugar cane, at a price of R14 000 an hectare. Thereupon the defendant said that he wanted R50 000 per hectare. Leo intimated that this was a ridiculous figure, but despite his expostulations the defendant refused to budge from his demand. The meeting ended inconclusively, Leo indicating that a deal might still be done if he could persuade BCM to pay the defendant a larger royalty. After Leo and Hooper had departed Townsend asked the defendant why he had put such a high figure on the extra

land. The defendant replied that he had done so "to block" JH and Townsend from selling their shares to BCM. He went on to say that in fact he wished to buy their shares for himself as he would like to have the controlling interest in the company for the reason that he enjoyed the quarry and that he had great plans for its expansion. The defendant then again offered JH and Townsend each R200 000 for their interests. They once more informed the defendant that this figure was unacceptable to them. According to JH the defendant responded to their refusal with the following statement:-

> "....he said that as he was wanting to run the quarry himself he was unable to pay us the same amount as Blue Circle because he required the capital for the day to day running and expansion of the plant and if he should pay us the full amount .... he would not be able to finance the quarry as he had intended."

The defendant then left the meeting.

Some days later Chaplin telephoned JH to tell

him that the defendant was prepared to offer JH and Townsend each R350 000 for their shares (in the case of Townsend the shares being those registered in the names of the daughters) and loan accounts in the company. JH and Townsend discussed the matter and decided to accept the offer. In the course of his evidence JH explained why he had decided to accept it:-

> "....there were a number of reasons .... The Defendant had repeatedly asked me and begged me to sell my shares to him. He had been up to Saxe Farm (JH's farm) and on other occasions and he made it quite clear to us on 29th after Mr Leo had left the meeting that this is what he wanted .... He was now talking a more realistic price. He'd come up from R150 000 to R200 000 to R350 000. He was after all .... part of our family. The quarry was situated on his farm and he had indicated to me at all times how much he liked the quarry .... He used the word he loved the quarry .... We did not think at that point in time that there were any other potential purchasers and in any event M'Lord had there been a purchaser to approach us we knew we would have to first offer our shareholding to the Defendant."

Townsend testified to the same effect. He stated his

reasons for selling to the defendant as follows:-

> "Well first of all .... he had come up from R200 000 to R350 000 which was a considerable increase. He had convinced us M'Lord that he wanted the quarry for himself, this being pointed out at the meeting .... after Mr Elmor Leo left, where he told us that he wanted the quarry for himself and he wanted to run it. He was after all a friend and Mr John Hulett a relation. We didn't see any other potential purchasers around and .... if we had a purchaser we would have to offer it to him first exactly as he would have to offer his shares to us."

(The obligation to afford fellow-shareholder the right of pre-emption to which both JH and Townsend referred, derived from a provision in the company's Articles of Association.)

Before their acceptance of the offer was communicated to the defendant the latter, on 2 March 1988, called on Ducray at the branch to show him the BMC H/A. From Ducray's advice form of that date the following appears:-

"Mr Hulett stated that he blocked the deal

through his strength of position in ownership of the Quarry Property .... He still intends to buy out his partners and requested us to open an account .... and permit him to overdraw up to R500 000.

.....

RECOMMENDATIONS

We recommend care and that we should not be bullied into agreeing to a further R500 000 exposure until some form of evidence can be furnished that one of the deals will definitely be proceeded with.

We mention that the Land Bank has agreed to assist Mr Hulett with a seasonal Loan of R410 000. This will alleviate some of his personal cash flow problems on the farming venture."

The evidence of a firm deal required by Ducray was soon provided. On 3 March 1988 the chairman of Bay Stone telephoned Ducray to inform him that in principle Bay Stone had agreed to purchase the company for R2 million "details to be worked out." On 4 March 1988 Todd addressed to the defendant a letter to the same effect. Todd expressed the hope that his letter would enable the

defendant to continue negotiations with the branch.

The fact that JH and Townsend had decided to accept the defendant's offer of R350 000 to each was communicated by JH to the defendant by telephone on 4 March 1988. The defendant's response to this news was described thus by JH in his evidence:-

> "He said 'I am so pleased that you have taken this decision because you know how much the quarry means to me and now I will get the control that I have been wanting.'"

It was agreed that the parties should meet in order to prepare a formal written contract for signature. Such a meeting took place in Chaplin's office on 7 March 1988. It was attended only by Chaplin, the defendant and JH who also represented Townsend. At the meeting a draft agreement ("the Chaplin draft") was drawn up by Chaplin. The defendant explained that either he himself or the trust would figure as the buyer in the agreement in its final form, and accordingly in the Chaplin draft the space

for the purchaser's name was left blank. In terms of the Chaplin draft the purchaser would pay R400 000 of the total purchase price of R700 000 against signature of the share transfer forms, and the balance of R300 000 on 28 February 1989. In his evidence JH described why payment of R300 000 was deferred. The defendant told them:-

> "....that he had borrowed R700 000 from the bank. However he could not make this payment in full because he required capital for the day to day running of Stanger Quarries to purchase new equipment and to up-date the old equipment. He then asked if we would be prepared to grant him a loan. This we agreed."

After further negotiation for the purpose of shaping Chaplin's draft it was agreed also that as security for the unpaid balance of R300 000 the defendant would give a bank guarantee. The drift of the defendant's remarks during these negotiations and his silence in the face of a pointed admonition by JH are significant. During his testimony JH recounted the discussions thus:-

"I asked him what security he would give us for the outstanding amount of R300 000. The Defendant's reply was that because we were friends and we knew him wouldn't we consider an unsecured loan. I said that I required something more business-like than that and in any event Mr Townsend had asked for suitable guarantees. I then said to the Defendant it was a very simple matter. I was quite happy if he was prepared to pledge the shares to us for a period of a year and when he finally made his payment on 28 February 1989 we would hand the shares to him.... He said he couldn't do this .... He said he wanted us to understand that if he ran into financial difficulties with the quarry....he might have to sell off some of the shares to generate cash....I said to him M'Lord that I fully understood his situation. However if he .... was dealing with somebody to sell off the shares at this point in time that we should know about that he should disclose it .... because if this did happen and Mr Townsend and I found out about it we would be very angry....It was a very casual statement M'Lord and the Defendant turned to me and said that he would prefer to give us a bank guarantee for the amount outstanding. This I accepted."

The purpose of the Chaplin draft was to enable Mr J M Koch ("Koch"), an attorney in Durban who acted for the trust, to draw up the contract in final form. A day or two

later Koch informed Townsend that the defendant had made arrangements with the bank which enabled him to pay the full purchase price in cash; and it was agreed between the parties that the contract would provide for such cash payment.

The contract was signed in Koch's office on 10 March 1988. Present were Koch, Galloway, the defendant, JH and Townsend. In terms of the contract the purchaser was the trust. The sellers were JH, Townsend and the daughters. In what follows reference to the individual daughters will be made respectively as "Paula", "Angela" and "Sally". The contract provided that the total purchase consideration of R700 000 was appropriated as follows:-

(1) JH's loan account R103 283,00

(2) Townsend's loan account ...103 283,00

(3) JH's 56 shares R246 717,00

(4) Paula's 19 shares 83 707,56

(5) Angela's 18 shares 79 301,88

(6) Sally's 19 shares 83 707,56

In clause 10.2 of the contract the following was stated:-

> "It is recorded and agreed that the purchaser is concluding this agreement with a view to obtaining control of the company and its operation...."

Upon signature of the contract, and after JH and Townsend had received their cheques, each in turn shook the defendant by the hand and congratulated him upon his acquisition of the quarry. To these gestures of goodwill the defendant responded by saying "Thanks a lot chaps. I'm sure if I go broke you two will come to my assistance."

Thereafter, and with great expedition, the assets which JH, Townsend and the daughters had sold for R700 000 in March were successively sold, first in April (by "the AFI agreement") to Attest Finance (Pty) Ltd ("AFI"), and then in May (by "the Bay Stone agreement") to Bay Stone.

In each case the purchase consideration was R2 million.

Both the AFI agreement and the Bay Stone agreement were drafted by Mr J Rabinowitz ("Rabinowitz"), a partner in a firm of attorneys in Johannesburg. Rabinowitz was also a witness at the trial. In drafting the two agreements Rabinowitz acted as the attorney of Bay Stone. It was necessary for him to confer with Koch in order to ensure that the agreements satisfied the requirements of Koch's clients. Rabinowitz told the court **a quo** that his mandate, and likewise that of Koch, was to minimise tax liability on the part of the parties to the agreements.

It is unnecessary to detail the elaborate scheme and structure of these two agreements which involved, **inter alia**, a dividend-stripping exercise.

In the AFI agreement, which was signed on 19 April 1988, the purchaser was AFI and the sellers were collectively the trust, McLelland and the SSC. As one

indivisible transaction:-

(1) the trust sold 112 shares (being the shares bought by the trust on 10 March 1988) for R493 430;

(2) the trust sold the 56 shares (originally acquired by it) for R997 332;

(3) McLelland sold his 18 shares for R200 000;

(4) the trust and the SSC sold all claims which the trust, the SSC and McLelland had against the company for R309 234.

The AFI agreement contained a restraint clause limiting for specified periods the quarrying activities of the defendant and McLelland within a 50 km radius of the Stanger Town Hall. In terms of the AFI agreement the SSC undertook to

enter into a further lease with the company (or Bay Stone) in terms of which the leased area was increased by 14,7475 ha. The rental for the lease was fixed at R100 per annum and the period of the lease was increased to 50 years from the 16 years then remaining under the original lease. The lease was to contain a clause precluding the erection of any structure within 100 meters of the perimeter of the leased land.

The Bay Stone agreement was concluded in May 1988 between AFI and Bay Stone. Pursuant to its terms:-

(1) the company was put into voluntary liquidation;

(2) the company awarded the quarry business to AFI as a liquidation dividend;

(3) AFI sold to Bay Stone the quarry business;

(4) the lease, as amended, was ceded to Bay Stone.

In due course news of the defendant's aforementioned transactions subsequent to 10 March 1988

reached the appellants. In July 1988 they instituted their action.

During the cross-examination of JH and Townsend defendant's counsel on a number of occasions sought to take issue with parts of their testimony by putting to them what the defendant himself as well as other witnesses to be called on his behalf would say in evidence. So, for example, it was suggested to JH that McLelland would testify that prior to 10 March 1988 he informed JH that Bay Stone directors had visited the quarry and that they had expressed interest in its purchase. This suggestion was firmly repudiated by JH. Suffice it to say that at the close of the appellants' case in the court below neither the defendant nor any witness on his behalf ventured into the witness-box.

In the course of his judgment the trial judge commented critically on an important aspect of Todd's

evidence. He remarked:-

> "....I am satisfied that Todd was less than frank in his evidence and that defendant had in fact asked him not to mention to Townsend the interest which Baystone Sales was showing in buying the shares in Stanger quarries."

There is nothing in the judgment of **Thirion** J which suggests that he was unfavourably impressed with the manner in which JH and Townsend testified before him. I would add that a careful reading of the record points to the conclusion that both were candid and careful witnesses.

The appellants rested their claim for damages on (1) positive fraudulent misrepresentation, and (2) fraudulent non-disclosure. In regard to (1), as will presently emerge, the trial court declined to accept the evidence of JH and Townsend as to the precise belief entertained by them on 10 March 1988 when they entered into the contract. Mr **Olsen**, who argued the appeal on behalf of the defendant, properly conceded that this adverse finding

by **Thirion J** was based purely on an assessment of the probabilities; and that in regard thereto this court was therefore in no less favourable a position than the trial court to make its own finding.

In his judgment the trial judge summarised his main findings of fact in the following words:-

> "On all the evidence and in the absence of any gainsaying evidence from the defendant I find that the plaintiffs have proved that when defendant signed the agreement on 10.3.1988.... :
>
> (i) he knew that Bay Stone Sales had offered in principle to purchase the shares in Stanger Quarries for R2 000 000;
>
> (ii) he knew that the plaintiffs and Townsend were ignorant of the Bay Stone offer and interest;
>
> (iii) he knew or believed that the Bay Stone offer for plaintiffs' shares was substantially more favourable than the price the Trust was offering the plaintiffs for their shares and which they were agreeing to accept by signing the agreement;
>
> (iv) he knew that plaintiffs and Townsend would not have entered into the agreement with the Trust if they had known or if they had been aware of

Bay Stone's offer and interest but that they would have tried to negotiate a sale of their shares direct to Baystone Sales;

(v) he knew that the plaintiffs and Townsend expected of him that he would disclose to them any offer which might influence their decision to sell their shares to him."

Following upon this passage in the judgment just quoted the learned judge proceeded to record a further finding of fact. For ease of reference I shall number it "(vi)". It was couched in the following words:-

(vi) "I find furthermore that defendant deliberately withheld from first plaintiff and Townsend all knowledge of Bay Stone Sales' interest and offer because he was afraid that if informed of it plaintiffs would not accept his offer but would endeavour to sell their shares direct to Bay Stone Sales."

At the end of the trial absolution was ordered. The main conclusions at which the trial judge arrived in his judgment may be summarised thus:

(1) that the appellants had failed to prove that any

possible fraudulent misrepresentation made by the defendant materially influenced JH or Townsend in making their decision to sell the shares to the trust;

(2) that the appellants had failed to establish a duty on the part of the defendant to disclose to the appellants the Bay Stone interest and offer;

(3) that in any case there was insufficient evidence to provide a basis for calculating damages.

Before examining more closely the reasons underlying the order of absolution it is useful to put into perspective what is a central feature in this case: the nature of the relationship between the members of the trio. This relationship would loom large in any consideration of the issue of fraudulent non-disclosure, but it is also germane to the issue of positive misrepresentation.

In the course of his judgment the learned judge remarked as follows:-

> Their longstanding friendship and association and previous dealings could have raised with plaintiffs the expectation that defendant would candidly disclose to them any offers which he received for the shares but this expectation was not one to which any obligation in law attached. There was no trust or confidence involved in their relationship such as would have legal consequences. Defendant did not receive knowledge of the Bay Stone offer and interest as agent for the plaintiff in a capacity where he acted on behalf of the plaintiffs. The offer was not made to the plaintiffs but to defendant."

In my respectful opinion the remarks quoted above represent too narrow a view of the facts and an incorrect statement of the legal principles governing them. For the reasons which follow it appears to me that the relationship subsisting between the members of the trio was in fact based upon trust and confidence, and that this situation entailed distinct legal consequences.

The strong personal ties at a social level which

bound together JH, the defendant and Townsend have already been described. After July 1984 their fates and fortunes were further linked in a joint business venture. In order to exploit the quarry they created a small domestic company in which they were co-directors, with equal loan accounts, and in which they personally or in a representative capacity had equal shareholdings. It is true that in some small domestic companies the association between the shareholders and directors may be purely commercial. However, in the case under consideration this was manifestly not the situation. For an instructive discussion of the topic, albeit in a different context, see the remarks of **Nestadt J** in **Erasmus v Pentamed Investments (Pty) Ltd** 1982(1) SA 178 (W) at 181-3. The evidence adduced on behalf of the appellants shows, so I consider, that the pre-existing personal bonds of mutual trust and confidence between the members of the trio was imported

into and sustained within the company. Apposite here is the reminder by **Lord Wilberforce** in **Ebrahimi v Westbourne Galleries Ltd** [1973] AC 360 (HL) at 379 B-C that a limited company is not merely a legal entity, and:-

> "....that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure."

In the instant case the picture which emerges from the evidence reveals that, within the external structure of the company, the relationship between the shareholders which existed internally was one which may be loosely described as a "quasi-partnership". A more precise legal tag need not be appended. The crucial fact of the matter is that the members of the trio themselves regarded the relationship as akin to partnership; that they described themselves as being partners; and that they appreciated that good faith is required from a partner in

his dealings with his co-partners. In **Wegner v Surgeson** 1910 TS 571 **Wessels** J said (at 579) that the relationship between partners is very much the same as that between brothers. In the present case nobody appreciated better than the defendant himself that during the continuance of a partnership one partner may not overreach his fellow-partners.

It will be recalled that in mid-1984, when the defendant mooted the idea of a consortium, JH expressed the wish to confine the number of participants in the venture which he described as "a partnership". Following upon a discussion between Townsend and the company's attorney, Brokensha, the latter on 24 February 1988 wrote a letter to the defendant. In this letter Brokensha, inter alia, affirmed:-

> "...that he [Townsend] felt that it was up to all the shareholders to be absolutely open and honest with each other and to keep each other fully posted as to any negotiations for the sale of

their interests, or of the total interests of the quarrying company, which might be taking place."

When on 12 February the defendant tried to raise a loan at the branch he explained to Ducray that he needed the money in order that he might make an increased offer "to his partners". The question of legal terminology apart, it is obvious that the defendant knew perfectly well that in the matter of the sale of shares in the company his conduct should be in accordance with the good faith and mutual trust on which the relationship between him and JH and Townsend was founded. It was the defendant's recognition of this truth which prompted him to describe to Ducray his surreptitious dealings with a third party as "unethical". Veritas, a quocunque dicitur, a Deo est.

The way has now been cleared for a closer look at the main reasons on which the order of absolution granted by the court below was based. It is common cause that at the time when the defendant was busy clinching the deal

with the third party for the sale of all the shares in the company for R2 million, the defendant was fraudulently misrepresenting to the appellants that if they sold their shares to him it was his intention to retain them in order to exercise control over the company and to continue to run the quarry business. It is also common cause that the defendant so misrepresented his state of mind in order to induce the appellants to sell their shares to him so that he might sell all the shares to the third party. At the outset it is necessary to make an assessment, having due regard to all the attendant circumstances, of the essential import of the defendant's misrepresentation.

In regard to the proper meaning to be assigned thereto the trial judge said in his judgment:-

> "In so far as the misrepresentation that defendant intended to retain the shares and control of Stanger Quarries, could be said to amount by implication to a representation that defendant did not know of any prospective purchaser interested in purchasing the shares,

> the difficulty in plaintiffs' way is that neither the first plaintiff nor Townsend said that he understood it that way. In any event I do not think that such an implication would be justified.

It seems to me, with respect, that the above remarks tend to overlook the true inquiry involved. The defendant knew that it was vital to the success of his stratagems that the appellants should be kept in ignorance of the fact that at that very time the defendant was engaged in furtive dealing with the shares in a third party. His misrepresentation was aimed at achieving this very result. The pertinent question is, therefore, whether or not by his misrepresentation the defendant in fact conveyed a message to the appellants that he was then not engaged in any such furtive dealing. Now it was a necessary postulate of such furtive dealing that there existed a prospective purchaser interested in buying the shares, and that the defendant knew of him. To this must be added that an intention to

keep shares for oneself is diametrically opposed to an intention to sell them. By his misrepresentation the defendant sought to convey to the appellants that he was not then engaged in furtive dealing concerning the shares with a third party. What he said to them carried that essential implication; and the evidence of both JH and Townsend makes plain that it was precisely thus that they understood the misrepresentation.

Once it is established that the appellants understood the misrepresentation as the defendant intended that they should, the remaining question on this part of the case is: Did such misrepresentation (together with the further misrepresentation in which the defendant had professed a powerful sentimental attachment to the quarry business) contribute to induce the appellants to sell their shares to the trust? In their evidence both JH and Townsend testified that they did. The trial court

concluded otherwise. The finding of the learned judge and his reasons therefor appear sufficiently from the paragraphs (numbered by me for easy reference) of the judgment quoted hereunder:-

(1) "I am ....unable to accept first plaintiff's and Townsend's evidence that when they entered into the agreement of sale with the Trust, they did so in the belief that if defendant had been aware of any offer from any third party to purchase the shares of Stanger Quarries or of any interest shown by a third party in purchasing the shares, he would have disclosed such interest or offer to them before concluding the sale with them.

(2) The defendant's conduct in relation to the Blue Circle offer must have made it quite plain to them that in the matter of the sale of the shares of Stanger Quarries defendant was selfishly and cynically pursuing his own interests and those of the Trust; that he was contriving by the use of all sorts of stratagems to depress the value of the plaintiffs' shares in order that in parting with its shares the Trust would either directly or indirectly obtain a correspondingly higher consideration for its shares."

(3) "When they concluded the agreement of sale with the Trust the plaintiffs knew that they were dealing with defendant at arm's length. Defendant's silence in the face of first

plaintiff's remark that if he was dealing with someone else who was interested in buying the shares he should disclose it, could only have heightened first plaintiff's and Townsend's suspicions that defendant was indeed dealing with someone else behind their backs. Indeed it would seem that the remark itself reflects first plaintiff's distrust of the defendant."

(4) "In my judgment plaintiffs have failed to prove that defendant's pretence that he wanted control of Stanger Quarries because of his fondness for the quarry business and that he intended to continue running the business played any part in their decision to sell their shares to the Trust. By the time that they came to sign the agreement of sale sentiment had ceased to weigh as a consideration with them."

The conclusion stated in paragraph (1) appears to be somewhat at variance with a finding earlier in the judgment of the trial court (in the paragraph numbered (v) already quoted by me) to the effect that the defendant knew that the appellants expected of the defendant that he would disclose to them any offer which might influence their decision to sell their shares to him. However that may be, I differ, with respect, from the learned judge's

conclusion in (1) which in my opinion runs counter to the evidence and the probabilities.

That during the abortive negotiations the defendant had demonstrated selfishness (see paragraph (2)) is perfectly true. But the fact that he was then obviously actuated by self-interest hardly served as evidence to his fellow-shareholders that he would stoop to deceit. It is likely, so I consider, that the defendant's intransigence over the BCM offer served merely as confirmation to the appellants of the defendant's oft-expressed determination to acquire control of the quarry business for himself.

The trial court's finding (in paragraph (3)) that at the time when the contract was concluded the appellants knew that they were dealing with the defendant "at arm's length" is, in my respectful opinion, untenable. It is based, I think, upon a faulty appraisal, both factually and

in law, of the true relationship between the members of the trio within the company. It may be that the silence which greeted JH's admonition to the defendant in Chaplin's office on 7 March 1988 should have alerted JH to the possibility that the defendant was dealing with someone behind the backs of the appellants; and in this respect perhaps JH displayed credulity. But in the witness-box both JH and Townsend stated that throughout their relations with the defendant they reposed complete faith in him; and I see no valid reason for doubting this evidence.

I further disagree with the finding (in paragraph (4)) that by the time that the contract came to be signed "sentiment had ceased to weigh as a consideration" with JH and Townsend. This conclusion fails to take into account, for example, their evidence, in this connection entirely unchallenged in cross-examination, of the congratulations extended by them to the defendant; and of the jocularity

simulated by the defendant in response thereto. In my view sentiment, genuinely entertained by JH and Townsend, runs through the case in an unbroken thread. To achieve his own ends the defendant traded upon and abused the bonds of sentiment and friendship. As an illustration I cite the fact that on 7 March the defendant advanced their friendship as a ground for making a loan of R300 000 by them to him interest-free.

In the present case a material representation was made which was calculated to induce the appellants to enter into the contract. There is evidence, which appears to be entirely credible, that the appellants were so induced. It seems to me that in these circumstances there arises a fair inference that this is in fact what happened. Mr Gordon who, with Mr Hewitt, appeared for the appellants, called our attention to one of the judgments delivered by the High Court of Australia in **Gould and Another v Vaggelas**

and Others, [1985] LRC (Comm) 497. The following remarks in the judgment of **Wilson** J (at 517 d-f) appear to me to indicate the proper approach to the situation here under consideration:-

> "Where a plaintiff shows that a defendant has made false statements to him intending thereby to induce him to enter into a contract and those statements are of such a nature as would be likely to provide such inducement and the plaintiff did in fact enter into that contract and thereby suffered damage and nothing more appears, common sense would demand the conclusion that the false representations played at least some part in inducing the plaintiff to enter into the contract. However, it is open to the defendant to obstruct the drawing of that natural inference of fact by showing that there were other relevant circumstances. Examples commonly given of such circumstances are that the plaintiff not only actually knew the true facts but knew them to be the truth or that the plaintiff either by his words or conduct disavowed any reliance on the fraudulent representations."

Here the defendant elected to adduce no rebutting evidence and in my view there is nothing before us which tends to displace the natural deduction that the appellants in fact

relied upon the fraudulent misrepresentation, as JH and Townsend said that they had done.

For these reasons it follows, in my judgment, that the trial court erred in deciding that the appellants had failed to prove that they were induced by the defendant's fraudulent misrepresentation to sell their shares to the trust. On this basis (subject to sufficient proof of the damages claimed) the appellants are entitled to succeed in this appeal. As a further string to their bow the appellants relied upon fraudulent non-disclosure by the defendant. Having regard to the nature of the relationship between the members of the trio it would be difficult, so I consider, to resist the conclusion that there rested a duty of disclosure upon the defendant. Upon this part of the case, however, it is unnecessary to make any finding, and I forbear from doing so.

It remains to deal with the matter of damages. The appellants are entitled to recover all losses which they have sustained as a direct consequence of having been induced by fraud to enter into the contract in terms of which they sold their shares to the trust. What must be restored to them is the amount by which their patrimonies have been diminished. The measure of damages is the difference between the price they received from the trust and the true market value of their shares on 10 March 1988. The market value is the price commanded by the shares in a fair market - the price determined as between a seller willing but not compelled to sell and a buyer willing but not compelled to buy.

In the instant case the market value of all the shares in the company is conveniently mirrored in the AFI agreement which was concluded only six weeks after the appellants had sold their shares to the trust. Mr Olsen

properly conceded that during this intervening period nothing had happened to alter the value of the shares. In connection with the measure of damages **Thirion** J remarked:-

> "The way I see it it would be taking too narrow a view simply to compare the purchase price which the Trust paid for plaintiffs' shares with the price which the Trust obtained for those shares in the sale to Attest and to ignore the other provisions of the sale between the Trust and Attest. It was a term of the sale to Attest that an additional 14,7475 ha of land adjacent to the quarry would be let by Sondela Sugar to Bay Stone Sales. Admittedly a separate rental was payable in respect of the lease of this land but it cannot be said that without having obtained this lease Attest would have paid the same price for the shares or would have purchased the shares at all."

The fact of the matter, however, is that AFI did, in a separate contract for an independent consideration, obtain the necessary lease; and that **ex facie** the AFI agreement it was the shares that AFI bought for R2 million. No reasons were advanced to us in argument why these

agreements should not be accepted at face value.

What does create a difficulty in the computation of appellants' damages, however, is the following. One is dealing here with shares in a private company. As a matter of commercial reality it must be recognised that in general a prospective buyer would be less disposed to purchase a portion only of its shares than he would be to buy its entire shareholding. A parcel of shares in a private company will, as a rule, command a lesser price per share than the price per share yielded by a sale of the entire shareholding. From this it follows that in the instant case the arithmetical calculation represented by $\frac{112}{186}$ x R2 million (i e the appellants' shareholding over the total issued shares) may be accepted as the market value of the appellants' shares only if it is safe to postulate that, had the defendant made full disclosure to JH and Townsend of the existence and interest of the third party,

all the shareholders would thereafter have sold all their shares to AFI for R2 million. As to this the learned trial judge expressed doubts. He said:-

> "The probabilities are that defendant would have employed the same tactics as those which he had employed to wreck the Blue Circle offer in order to obtain a higher price for the shares of the Trust than the price which plaintiffs would have obtained for their shares or that he would have stipulated an exorbitant price for the additional land.

I respectfully disagree with this view of the matter. Having due regard to the evidence I consider that a strong balance of probabilities points to the conclusion that all the shareholders would have sold the entire shareholding to AFI on the same terms and conditions; and at the same price. It must be remembered that when in October/November 1987 BCM displayed renewed interest in the company the defendant was not unwilling to sell. His attitude was simply that the BCM offer was too low. By February 1988, it is true, he was no longer interested in

selling to BCM; but his change of attitude was dictated by the fact that at that stage he knew that Bay Stone was waiting in the wings. In weighing the probabilities the defendant's overall financial position and his state of mind in regard to the options open to him at the time are significant. On 10 February 1988 Ducray's assessment of the defendant's financial position was that he was "over extended". On 18 February 1988 the defendant told Ducray that if the M & R deal fell through he could fall back on the BCM offer, and that "at worst" he could himself continue with the quarry. On the same day Ducray reported to the GM that the defendant was unable to continue with the quarry without further finance. As appears from Ducray's report to the GM on 2 March 1988, the defendant had cash flow problems in his farming venture. It is possible, of course, that for some or other reason not apparent from the record before us, the defendant might

have been disinclined to join with all his fellow-shareholders in selling the entire shareholding to AFI. But the defendant preferred not to testify, and it is not for this court to indulge in speculation on the point.

For the aforegoing reasons it seems to me not only that there was sufficient evidence before the trial court to provide a sufficient basis for calculating the damages suffered by the appellants as a result of the defendant's fraudulent misrepresentation, but further that the method of computation set forth in the particulars of claim represents a realistic and just measure of the appellants' loss and the defendant's corresponding gains.

The record of the proceedings in the court below was filed late with the registrar of this court. The delay involved is, we consider, largely the fault of the respondent's Durban attorney. The application for

condonation was not opposed, and counsel were agreed that the costs thereof should be costs in the appeal. The application for condonation is well-founded.

The late filing of the record is condoned. The appeal succeeds with costs, such costs to include the costs of two counsel, and the costs of the application for condonation. The judgment of the court **a quo** is altered to read:-

> "Judgment is granted against the defendant with costs, including the costs of two counsel, as well as those costs occasioned by an adjournment of the trial on 18 April 1989, in the following amounts:
>
> (1) for the first plaintiff in the sum of R250 205,00;
>
> (2) for the second plaintiff in the sum of R84 890,98;
>
> (3) for the third plaintiff in the sum of R80 423,03;
>
> (4) for the fourth plaintiff in the sum of R84 890,98."

G G HOEXTER, JA

VAN HEERDEN, JA)
NESTADT, JA)
MILNE, JA) Concur
NICHOLAS, JA)