IN THE HIGH COURT OF SOUTH AFRICA
(CAPE OF GOOD HOPE PROVINCIAL DIVISION)

Case no.: 8055/2002

In the matter between:

YVETTE JOAN FARREN Applicant

and

SUN SERVICE SA PHOTO TRIP MANAGEMENT (PTY) LTD Respondent
(Registration No. 87/04411/07)

JUDGMENT GIVEN THIS WEDNESDAY, 16 APRIL 2003

CLEAVER J:

[1] This is an application to compel specific performance by the respondent of the terms of a written agreement of sale concluded with the applicant on 27 August 2002. In terms of the agreement, the respondent sold the immovable property known as 39 Skaife St, Scott Estate, Hout Bay ('the property') to the applicant for a purchase consideration of R1 450 000.

[2] In a communication by e-mail on 13 September 2002 the applicant was informed by the sole director of the respondent that the respondent would no longer sell the property to the applicant. This prompted the application before me which was brought as a matter of urgency on 24 October 2002. The applicant seeks an order directing the respondent to take the necessary steps to sign the requisite documentation to pass transfer of the property to the

applicant, it being common cause that the applicant has made provision to pay the deposit of R100 000 due in terms of the deed of sale and has obtained a loan to be secured by a mortgage bond over the property for the amount specified in the agreement of sale. In terms of the order granted on 24 October 2002 the respondent has been interdicted from dealing with the property pending the hearing of the application.

[3] Respondent has raised the following defences to the application, namely

1) That the applicant is not entitled to the relief sought because in terms of a written addendum concluded by the parties on 27 August 2002 it was agreed that instead of taking transfer of the immovable property, the applicant would acquire the shares in the respondent, which is the owner of the immovable property.
2) That the agreement did not bind the respondent and is not a valid agreement because the approval of the shareholders to the deed of sale had not been obtained in accordance with the provisions of section 228 of the Companies Act.

Certain other defences were alluded to in the respondent's answering affidavit, but were ultimately not pursued.

THE ALLEGED AGREEMENT TO ACQUIRE SHARES IN THE RESPONDENT.

[4] The addendum to which I have referred reads as follows:

"ADDENDUM TO OFFER TO PURCHASE
39 SKAIFE STREET, HOUT BAY ERF: 4939

It is the purchaser's intent to purchase the PTY Company in which the sole asset is the property known as 39 Skaife Street, Hout Bay Erf: 4939

The seller hereby warrants to give all relevant documentation such as financials within Ten (10) working days, when called to do so by the Transferring attorneys.

Both the seller and the purchaser hereby undertake to sign all relevant documentation to bring to successful conclusion, the sale of the above-mentioned property."

(I would mention that although the property is reflected as Erf 4939 in the addendum, it is reflected to as Erf 4875 in the Notice of Motion. I have assumed that the latter is the correct description.)

[5] Mr **Marais**, who appeared on behalf of the respondent submitted, if I understood him correctly, that the application was premature because the addendum, properly interpreted, brought about a new contract in terms whereof the nature of the agreement was altered. I do not agree that this is the interpretation to be placed on the addendum. In my view its meaning is plain. After concluding the agreement of sale, the applicant had in mind to purchase the shares in the company owning the property, if possible. Although an agreement for the sale of the property had been concluded, the parties agreed that if the applicant still wished to purchase the shares in the company once she had received financial statements and other relevant documentation of the company, they would sign the necessary documents for the sale of the shares. It is thus an agreement in principle to sign another agreement, but it is implicit in my view that the parties would only proceed to sign another agreement if the applicant wished to do so, once she had had sight of the financial statements of the company and its other relevant documentation. Whether the addendum

would have been sufficient to constitute a binding agreement once the applicant had been satisfied as to the financial state of the company and its documentation is not an issue I have to decide. The respondent repudiated the agreement to sell the property on 13 September. That repudiation was not accepted by the applicant who now asks that effect be given to the original agreement. In doing so she has elected not to pursue her intention to alter the original agreement (an option which would have been for her benefit) and in my view she is perfectly entitled to adopt this course.

SECTION 228

[6] Section 228 of the Companies Act reads as follows

> "228. ***Disposal of undertaking or greater part of assets of company.***---
> *(1) Notwithstanding anything contained in its memorandum or articles, the directors of a company shall not have the power, save with the approval of a general meeting of the company, to dispose of --*
> *a) the whole or substantially the whole of the undertaking of the company; or*
> *b) the whole or the greater part of the assets of the company.*
> *(2) No resolution of the company approving any such disposal shall have effect unless it authorizes or ratifies in terms the specific transaction.*
> *(3) The requirements contained in this section in respect of transactions falling within the provisions of subsection (1), shall be in addition to any other requirements, including the limitation of voting rights, relating to such transactions that may be imposed by the Securities Regulation Panel in terms of section 440C or in terms of any other law."*

[7] It is common cause that the approval of the shareholders of the respondent in general meeting has not been obtained for the disposal of the property, which, on the uncontroverted evidence tendered on behalf of the respondent, is the

sole asset of the respondent. It is also common cause that Anya Elisabeth Klages ('Klages'), who signed the agreement of sale on behalf of the respondent, is the sole director of the respondent. She holds a very minor interest in the company, namely 20 of the 30 100 issued shares with the bulk of the shareholding being held by a German company controlled by her mother. The capacity in which Klages signed the agreement of sale on behalf of the company is not apparent from the document. Although I have referred to the document as an agreement of sale, it took the form of an offer to purchase addressed by the applicant to the respondent. It contained a clause to the effect that when the offer was accepted the agreement would constitute the entire agreement between the parties. The agreement thus came into being when Klages signed the document signifying acceptance of the offer. This she did by signing her name above the reference to *"seller"* in the acceptance clause. It is not disputed that in doing so she purported to act for the seller and, as she is the sole director of the seller, I will accept for the purposes of this matter that she had the implied authority to conclude an agreement for the disposal of the seller's property on behalf of the seller. The transaction was accordingly *intra vires* the company. The reliance on section 228 appears in a further (second) affidavit filed by Klages in which she avers that she did not have the power to conclude a sale of the property to the applicant or to anyone else and states

> *"That there was no general meeting of the respondent called or held to approve or ratify such transaction. Furthermore, the transaction was not so approved, and the shareholders have not subsequently approved or ratified any sale of the property, or shares in the respondent."*

[8] The line of defence raised by the respondent brings into sharp focus the dichotomy which exists between the provisions of section 228 of the Companies Act and the so-called *Turquand* rule, which has long been a part of our company law. The rule derives from *Royal British Bank v Turquand* (1856) E&B 248(119 ER 474) (confirmed on appeal in 6 E&B 327 (119 ER 886)) and was accepted as part of our law in *The Mine Workers' Union v J J Prinsloo; The Mine Workers' Union v J P Prinsloo; The Mine Workers' Union v Greyling* 1947 (3) SA 831 (A). The rule is generally expressed by saying that a person dealing with a company in good faith is entitled to assume that all internal formalities or acts of management have been duly performed and carried out by the company.

[9] In *Rolled Steel Products (Hldgs) Ltd v British Steel Corp B S & C* 1986 Ch 246; 1985 (3) All ER 52 (CA) at 285; 78 it was held that the person invoking the rule was at least obliged to plead that he did not know of the irregularity and was entitled to assume that the relevant provisions of the companies' constitution had been properly and duly complied with. The applicant's founding papers contain no such allegations, but in fairness to the applicant, the section 228 defence appears to have been raised for the first time only in the respondent's answering affidavit. In reply thereto the applicant says

> *"it is significant to note that in addition to being the sole director of Respondent and confirming her authority to depose to an affidavit on a Respondent's behalf, Klages describes herself as a seller of the property as will more fully appear from annexure 'YJF1' to which this Honourable Court is respectfully referred. I submit with respect that the inescapable conclusion therefrom is the fact that at all time material hereto Klages represented that she had the necessary authority to bind the Respondent herein."*

Further on she says that:

> *"…Klages has at all times material hereto held out that she had authority to bind the Respondent and until now has never stated that she lacked and/or required authority to negotiate and conclude the agreement."*

Although one may have expected the applicant to record more clearly that she

did not know of the irregularity and was entitled to assume that the relevant provisions of the company's constitution had been properly and duly complied with, I will accept that the applicant's averments, however scanty, are sufficient.

[10] It now seems to be generally accepted that section 228 of the Companies Act (and its predecessor, section 70*dec*(2) of the 1926 act) was introduced for the protection of the shareholders in a company who have placed the control of the company in the hands of its directors.

Sugden and Others v Beaconhurst Dairies (Pty) Ltd and Others 1963 (2) SA 174 (E) at 179G; and *Levy and Others v Zalrut Investments (Pty) Ltd* 1986 (4) 479 (T) at 485B.

In *Lindner v National Bakery (Pty) Ltd and Ano* 1961 (1) SA 372 (O) the court reasoned that the object of section 70*dec*(2)

> "…appears to be to prevent the directors from obtaining a general authority to enter into any agreement for the disposal of the undertaking of a company or of the whole or greater part of its assets as they, the directors, might in future deem advisable. *The object of the section is therefore evidently that the shareholders are to exercise control over the disposal of the undertaking or greater part of the assets of the company."*

(At 379C-D)

[11] In my view it is clear that the mere fact that the agreement had not been authorised or approved by the shareholders does not make it invalid or void. This must be so because section 228 (2) makes provision for the subsequent ratification of an agreement by shareholders. In this connection I am in respectful agreement with the view expressed by **Magid** J in *Ally and Others NNO v Courtesy Wholesalers (Pty) Ltd* 1996 (3) SA 134 (N) at 145E-G. The question, however, is whether I am entitled to order the respondent to pass

transfer of the property in the absence of the resolution prescribed by section 228. I am not aware of any case in which a court has ruled definitively on whether an innocent purchaser should be protected where the transaction was, as in the present case, *intra vires* the company, but without the authority or approval of the shareholders as required by section 228. There is however strong support for this view in an *obiter* portion of the judgment of **Van Zyl** J in *Levy and Others v Zalrut* at 487B-D:

> "There is likewise no indication that the public interest or public policy played any part in the intention of the Legislature when it enacted the said s 228. A third party involved in a transaction relating to the said disposal will hence undoubtedly be able to enforce such transaction, provided he is not aware thereof that the company in general meeting has in fact not approved of the transaction. This is in accordance with the rule in the well-known case of Royal British Bank v Turquand *(1856) 5 E&B 248 (119 ER 474) (confirmed on appeal in 6 E&B 327 (119 ER 886)), which was accepted as part of our law in* The Mine Workers' Union v J J Prinsloo*;* The Mine Workers' Union v J P Prinsloo*;* The Mineworkers' Union v Greyling *1948 (3) SA 831 (A)."*

[12] The judgment of **Van Zyl** J in *Levy and Others v Zalrut* gave rise to a flurry of academic writings, all of which highlighted the problem which exists if the *Turquand* rule is to apply to circumstances hit by the operation of section 228. In a note on the case published in THRHR 1987 (50) at 226 Prof P E J Brooks raised the question as to whether the application of the rule in the context of section 228 is reconcilable with the conclusion reached by **Van Zyl** J that the section *"is clearly directed at protecting the interests of shareholders".* After all, a decision to enforce a contract concluded without the approval of or ratification by any shareholders in general meeting can hardly be said to be in the interests of those shareholders who do not approve it. This was followed by an article

entitled *"Die Uitwerking van artikel 228 van die Maatskappywet 61 van 1973 op die Turquand Reël* by Michele von Willich in 1998 Modern Business Law 7. This article, which was based on the author's LLM thesis contains a valuable summary of the law in England, Canada, France, the Netherlands and Germany and highlights the fact that only Canada has a statutory provision similar to our section 228. She also sketches the background to the introduction of section 228 in the statute. Section 70*dec*(2) of the Companies Act No 46 of 1926 contained provisions almost identical to section 228 and in a note published in 1971 SALJ at 351, Basil Wunsh, writing prior to his elevation to the bench, expressed the view that

> ***"The approval of a general meeting of a company required by s 70 dec(2) is an 'act of internal management' and the case of directors disposing of the undertaking of a company without such approval is indistinguishable from the position in Turquand's case, save that the limitations on the directors' powers are derived from the statute."***

His view was therefore that an innocent party contracting with a company would be entitled to invoke the provisions of the rule notwithstanding section 228. A similar view was expressed by Prof M J Oosthuizen in a note on *Novick and Another v Comair Holding Ltd and Others* 1979 (2) SA 116 (W) published in 1979 TSAR at 169.

Von Willich concludes her treatise by returning to the cardinal issue to which regard must be had when interpreting statutes, namely the intention of the legislature. She points out that transactions which are forbidden by statute are *prima facie* considered to be void (in accordance with the maxim *quid fit contra legem est ipso iure nullum*) but accepts that the intention of the legislature could also be that although the transaction may be forbidden, it is not necessarily visited with voidness. In this connection, she refers to the interpretation given to section 141 of the Companies Act, namely that an offer of shares to the public for purchase without being accompanied by a written statement containing certain prescribed information will not be void. Since the contravention of section 141 is also an offence, she argues that

contravention of section 228, which is not an offence, should also not be regarded as being void. In attempting to establish the intention of the legislature, she submits that since the *Turquand* rule had become firmly established in our law, the legislature would have made it clear that an innocent third party would not be entitled to rely on the rule had that been the intention of the legislature. She concludes by submitting that in weighing the interests of the innocent third party against those of the shareholders, the interests of the former should prevail since the wronged shareholders would be entitled to claim damages from the errant organ or agent of the company for breach of fiduciary duty. In her view section 228 should be repealed.

[13] The opposite view is taken by Prof J S A Fourie in an article entitled *"Verkoop van die onderneming van die maatskappy – het artikel 228 van die Maatskappywet nog betekenis?"* published in TSAR 1992-1. For him, as for Von Willich, the answer is to be found in the intention of the legislature enacting section 228. I agree with him that the issue is not so much whether a transaction entered into in contravention of section 228 is void or voidable. It is clearly unlawful in the sense that it is concluded in contravention of the section; it also has no legal effect, but that can be cured by subsequent ratification by the shareholders in general meeting.

[14] If it is accepted that the objective of the legislature was to protect the shareholders, then surely that intention should be given effect to, for otherwise *"admitting the application of the* Turquand *rule may resolve the dilemma, but will nullify the efficacy of section 228 and will defeat the object of the legislature"* (L Hodes – *"Disposal of assets – s228"* 1978 The South African Company Law Journal F-6, F-13). As pointed out by Prof Fourie, Von Willich's view, by implication, is that the legislature intended to curb the authority of directors well knowing that the *Turquand* rule would effectively neutralise the provisions of

section 228 and that this could never have been the intention. I agree.

[15] Supporters of the view that the *Turquand* rule should prevail argue that if the provisions of section 228 had been contained in the articles of association of a company, an innocent party would have been entitled to invoke the rule. Therefore, since the provisions of section 228 amount to nothing more than internal arrangements which are to be complied with by the directors, they should be treated in the same way in which they would have been treated had they been contained in the articles of association. In my view this is too simplistic an argument. For reasons which the legislature considered sound, it was decided that the provisions in question should be embodied in a statute, thus giving them far more weight. In *Lindner National Bakery the* court expressed itself as follows in regard to section 70*dec*(2) of the previous act:

> "On the other hand it is difficult to escape the argument that where the Legislature, in order to achieve its object that the directors shall not sell without the consent of the shareholders, has laid down in clear terms the procedure to be followed when a company seeks to sell its undertaking or the greater part of its assets, that procedure must be followed, even though the consequences of giving effect to the prescribed procedure may be such as to justify the surmise that Parliament did not appreciate the full effect of its pronouncement. See Rex v Bennett and Co. (Pty.) Ltd. and Another*, 1941 T.P.D. 194 at p. 200."*
> (At 380A-B)

[16] In a further article on section 228 and the *Turquand* rule in TSAR 1992-3 at 545 Basil Wunsh repeated his earlier view as to section 70*dec*(2) of the previous act. In addition to points made in the earlier article, he submits that the following factors should also be taken into account and reinforce his view that the rule should prevail over the provisions of the statute:

1) The absence of a penalty.

2) The *ratio* of the *Turquand* rule and the general application of the presumption *omnia praesumuntur rite ac solemniter esse acta* as a rule of substantive law.

3) That there are no considerations of policy or public interest involved.

As to (1), the absence of a prescribed penalty in the event of a statutory contravention is often taken to be an indication that no public interests are involved, but to my mind that fact does not tip the scales in favour of the *Turquand* rule in the circumstances under discussion. I also do not agree that in relation to section 228 it can be said that the *omnia* presumption applies equally to section 228 as it does to the internal arrangements of the company, for this argument also disregards the intention of the legislature.

[17] Some proponents of the rule argue that since the section was introduced for the protection of the shareholders of a company, the rule should prevail since there are no public interests involved. This is the view of Prof Blackman in his chapter on companies in LAWSA Vol 4 Part 2 (First Reissue). But, as Prof

Fourie has pointed out, sections 220-234 of the act all contain provisions which curtail the powers of directors. The *Turquand* rule was not relied on in *Neugarten and Others v Standard Bank of South Africa Limited* 1989 (1) SA 797 (A), in which the court held that sections 226(1) and (2) were introduced solely for the protection and benefit of the members of a company. The section prohibits a company directly or indirectly from making certain loans or providing security to or for a director or manager of itself or of its holding company or of another subsidiary of the holding company without the consent of all the members or the passing of a special resolution. Wunsh seeks to distinguish the judgment from the situation when it is attempted to invoke the *Turquand* rule so as to override section 228 for the following reasons.

1) Section 226(4) of the act makes the errant director of officer guilty of an offence;
2) Without the prescribed consent or special resolution the transaction are *ultra vires* the company;
3) The mischief aimed at is far more serious that at which section 228 aims; and
4) The validating formality is the written consent of all the members which can easily be called for and produced; or a special resolution which is registered and is such is a public document.

Whatever value the points put forward by Wunsh may have, they are not in my view a sufficient indication that it was the intention of the legislature to permit the *Turquand* rule to prevail over the provisions of the section. In this regard I consider that the following passage from the judgment of E M **Grosskopf** JA,

who delivered the majority judgment in *Bevray Investments (Edms) Bpk v Boland Bank Bpk en Andere* 1993 (3) SA 597 at 622 *in fine* to 623D to be particularly instructive.

> "Die reël dat die Wetgewer se bedoeling in eerste instansie in die letterlike betekenis van sy woorde gesoek word is so geyk, en die redes daarvoor so klaarblyklik, dat dit skaars beklemtoning verg. Die Wetgewer bepaal wat veroorloof word en wat verbied word. Die onderdaan kan alleen die Wetgewer se wil vasstel uit die woorde wat gebruik word. In ´n geval soos die onderhawige, as ´n direkteur of ´n maatskappy-sekretaris of ´n ouditeur wil weet of ´n bepaalde lening ´n oortreding van art 226 is, behoort hy die antwoord te kan vind in die woorde van die Wet, en, indien hulle duidelik is, behoort dit nie vir hom nodig te wees om te bespiegel of die Wetgewer nie miskien iets anders bedoel het nie, of om rond te krap in die wetgewende *geskiedenis van die bepaling nie. Daar word gevolglik dikwels beklemtoon dat dit net in uitsonderlike gevalle is waar afgewyk mag word van die letterlike betekenis van die woorde van wetsbepalings—'(s)legs ´n duidelike en onbetwyfelbare bepaalde bedoeling van die Wetgewer, en nie ´n bloot veronderstelde bedoeling nie, kan ´n afwyking van die gewone betekenis van woorde regverdig…' (*per *Botha AR in* Du Plessis v Joubert *1968 (1) SA 585 (A) op 595A). Sien ook* S v Tieties *(*supra*) op 464A: '…a Court…may only do so where this is necessary to give effect to what can with certainty be said to be the true intention of the Legislature' en op 464E 'provided it can be indisputably established that the Legislature intended something different from the ordinary meaning conveyed by the words used…"*

In my view it cannot in the present case be indisputably established that the legislature intended something different from the ordinary meaning conveyed by the words used. I must therefore respectfully disagree with the *obiter* remarks by **Van Zyl** J in *Levy and Others v Zalrut* inasmuch as they can be said to support the application of the *Turquand* rule so as to negate the provisions of section 228. In my view the legislature intended the provisions of the section to prevail.

[18] In conclusion I should add that a major part of the applicant's case as argued before me was that she was entitled to succeed on the grounds of estoppel, the submission being that because Klages brought the applicant under the impression that she was entitled to bind the respondent the respondent was estopped from denying her authority. This is of course not the test for estoppel – it is only the principal's actions which can give rise to estoppel being raised against the principal. While it could have been argued that by appointing Klages as the sole director and allowing her to act for the company, the respondent had created the impression that she could bind the company, the onus to be discharged in order to establish estoppel is far greater than that which is necessary to establish the operation of the *Turquand* rule. It is in my view in any event not necessary to go into the issue for as pointed out by Prof Fourie the general principle, as formulated in LAWSA is

> "Estoppel is not allowed to operate in circumstances where it would have a result which is not permitted by law. A defence of estoppel will therefore not be upheld if its effect would be to render enforceable that what the law, be it the common law or statute law, has in the public interest declared to be illegal or invalid." (Para 387)
> (Now in Volume 9 (first re-issue) at para 470.)

See also *Strydom v Land-en Landbou Bank* 1972 (1) SA 801 (A) in which the Appellate Division held that estoppel will not be permitted if by doing so a result would be achieved which is contrary to the intention of the legislature. As far as section 228 is concerned, an agreement concluded on behalf of the company in contravention of the section has no legal effect unless and until it is ratified by the shareholders. If the *Turquand* rule cannot apply, then for the same reason, estoppel cannot apply.

In the circumstances the application is dismissed with costs.

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R B CLEAVER