IN THE HIGH COURT OF SOUTH AFRICA
(Cape of Good Hope Provincial Division)

REPORTABLE
Case No. 6859/2002

In the matter between

M A VLEISAGENTSKAP CC **First Plaintiff**
WESTERN PROVINCE MEAT SUPPLY BK **Second Plaintiff**

And

BRYAN NEVILLE SHAW N.O. **Defendant**

JUDGMENT: DELIVERED ON 15 OCTOBER 2003

DAVIS J

Introduction.

Plaintiff issued summons against defendant in his capacity as trustee of the insolvent estate of Harry Sacks ('Sacks'). Plaintiff basis its claim in terms of section 64(1) of the Close Corporations Act 69 of 1984 ('the Act') and seeks to establish personal liability on the part of Harry Sacks by reason of his carrying on of the business of Sacks and Sons CC (in liquidation) in a reckless, alternatively grossly negligent manner with intent to defraud creditors. In the alternative, plaintiff seeks damages from defendant based on a common law action for misrepresentation.

The background to this action can be summarised thus:

The plaintiffs are wholesalers who sold meat for a number of years to Sacks and Sons CC ("the close corporation"). The close corporation was placed under a provisional order of

liquidation on 18 September 2000 and the order was made final on 17 October 2000. The liquidator of the close corporation brought an action for the sequestration of the estate of its majority member, Sacks based on the latter's debit loan account in the amount of R2 865 720,00. Sacks' estate was provisionally sequestrated on 24 October 2000 and finally sequestrated on 5 December 2000. Defendant was appointed as the provisional trustee of the debtor's estate and subsequently as trustee thereof. First plaintiff proved a claim against the close corporation in liquidation on 20 February 2001 in the amount of R588 696,18 for goods sold and delivered. On the same date, second plaintiff proved a claim against the close corporation in liquidation in the amount of R63 918,19 for goods sold and delivered.

Claim forms were deposed to by Hendrik Reneé Ahlers on 21 December 2001 on behalf of plaintiffs. It was recorded in paragraph 5 thereof that no person beside the said estate was liable for the debt or any part thereof. On 24 April 2001 Ahlers deposed to a claim form on behalf of plaintiffs in which identical amounts were claimed from the insolvent estate of Sacks for goods delivered. These claims were proved against Sacks' insolvent estate. Upon receipt of the invoices in respect of the goods sold and delivered, defendant became aware that the goods had in fact been sold and delivered to the close corporation. Defendant accordingly applied to the Master to have the claims expunged and this was duly done in terms of section 45(3) of Act 24 of 1936 on 5 March 2002.

In March 2002 plaintiffs launched an application in which they sought an order declaring

that defendant in his capacity as trustee of Sacks' insolvent estate was liable for the debts of the close corporation in the sums of R588.696,18, and R63.918,70 respectively. This application was subsequently withdrawn, and plaintiffs agreed to pay defendant's costs. The present action was then instituted in September 2002.

The Claims.

In its main claim first plaintiff claimed that during the period 21 August 2000 to 15 September 2000 the close corporation, represented by Sacks, ordered a quantity of meat. First plaintiff further alleged that during this period Sacks conducted the close corporation's business recklessly and/or with gross negligence and/or with the intention to defraud first plaintiff in that Sacks ordered and took delivery of meat while knowing that the close corporation was insolvent and that it accordingly would not be able to pay for it. It is alleged in its pleadings that Sacks fraudulently advised first plaintiff that the close corporation would pay for the meat. During this period Sacks wrote out cheques on behalf of the close corporation which he knew could not be honoured. He further alleged that Sacks conducted the business in a reckless and/or gross negligent manner and the close corporation incurred substantial new debts during the relevant period while Sacks knew or should reasonably foreseen that the close corporation was at that stage insolvent and could not pay any new debt. First plaintiff therefore alleged that the value of the meat in question amounted to R588 696,18 and that first plaintiff had not received payment in respect thereof.

Second plaintiff's main claim is identical to that of first plaintiff save that it relates to the

period 4 September 2000 to 15 September 2000 and the value of the meat is said to be R63 918,70.

Both plaintiffs instituted an alternative claim on the basis that during the relative period Sacks intentionally defrauded and misrepresented that the close corporation would pay for the meat. Plaintiffs allege that the misrepresentation was false and that Sacks knew that the plaintiffs would receive no payment in respect thereof. They further allege that the misrepresentations were material and made by Sacks with the intention to persuade plaintiffs to deliver meat to the close corporation and further that plaintiffs were so induced.

Evidence.

Plaintiffs called two witnesses, one Gerhard Snyders and Ahlers. Snyders testified that, as the erstwhile manager of Rainbow Meat Wholesalers ('Rainbow') on the Friday preceding the Monday on which an urgent application was brought for the liquidation of Sacks and Sons CC, he received an order from Sacks to deliver meat to the close corporation. He explained that early on Monday 18 September 2000 he received a call from Sacks during which Sacks impressed upon him the urgency of the delivery of the meat which had been ordered on Friday. Thirty sides of meat were accordingly delivered to the close corporation by Rainbow Meat Wholesalers.

On 18 September 2000 between 10h00 and 11h00 the owner of Rainbow, Mr Prinsloo,

informed Snyders that an urgent application for the liquidation of the close corporation was scheduled for 14h00 on that day and that the meat which Rainbow had delivered to the close corporation had to be recovered before the latter went into provisional liquidation. When Snyders arrived at its premises, the staff of the close corporation had already started cutting up the meat which Rainbow had delivered earlier that day. After initial resistance, Snyders managed to regain possession of the meat after Sacks agreed that the product could be removed.

Ahlers testified that he had built up a close business relation with Sacks over a period of forty years. A month prior to the liquidation of the close corporation Sacks had assured him that the close corporation was doing good business and that it had signed a new and favourable contract. Ahlers testified that even when prompted about the apparent lack of profitability of the Waterfront branch of the close corporation, Sacks maintained that the business had not experienced significant financial problems and indeed was conducting a profitable business. Ahlers explained that on Friday 15 September 2000 certain cheques were collected from Sacks for meat delivered in the preceding fourteen day period as well as post-dated cheques for meat delivered to the close corporation for the week ending Friday 15 September 2000. He testified that certain cheques had been post-dated to a date too far ahead and that, following a request by him to this effect, Sacks had changed the dates on these cheques in Ahlers' presence to a date closer to 15 September 2000. Ahlers explained that a cheque which was dated for 12 September 2000 had been handed to him by Sacks with the assurance that, if presented for payment on 15 September 2000,

it would be honoured.

He further testified that Sacks failed to disclose to him that the close corporation had been incurring a loss in an amount of R30,000 per month for a portion of the leased property which the close corporation could not use itself and which it had failed to sub-let. He had also failed to disclose that the close corporation had incurred losses at its Mitchell Plain's branch by reason of an opposition meat retailer who opened a shop in the same area, or that the close corporation had liabilities exceeding its assets by more than R8 m.

Ahlers testified that for the past ten years cheques had been collected on a Friday in respect of the purchases for the period two weeks prior thereto. He stated that the last purchases by the close corporation were on 13 or 14 September 2000. However he did say that a transaction might have taken place on the Friday 15 September because 'Soos ek vantevore gesê het ons probeer om ons voorrade tot nil te kry op 'n Vrydagoggend en hierdie moes die laaste goed gewees het wat ons gehad het of hulle was Donderdag bestel en Vrydagoggend vroeg uit gestuur of ons het hom Vrydagoggend genader en gesê help ons asseblief, ons het nog voorraad wat ons ontslae van wil raak. Hierdie aflewering sou vroeg in die oggend geskiet het'

Plaintiffs' Case.

Mr Potgieter, who appeared together with Mr Fourie on behalf of plaintiffs, submitted

that the evidence of Snyders and Ahlers constituted **prima facie** proof of the fact that Sacks had carried on the business of the close corporation in a reckless or grossly negligent manner. The evidence of Snyders, in particular to the effect that Sacks wanted an urgent delivery of meat as early as Monday morning despite the fact that he knew that the close corporation on whose behalf he sought to take such delivery would be liquidated at 14h00 on that day, constituted **prima facie** proof that Sacks had conducted the business of the close corporation recklessly or with direct intent to defraud creditors.

He submitted that the evidence of Snyders and Ahlers must be measured, not only against the timing of the application for liquidation and Sacks' conduct at the time, but against the explanations offered by Sacks as well as the liquidator's report.

Mr Potgieter placed considerable emphasis on the founding affidavit of Sacks to which the latter had deposed in support of the application for the liquidation of the close corporation. In that affidavit Sacks stated 'It has now become clear that the Applicant has no alternative but to move for the winding up of the Applicant. The Applicant has no funds to carry on servicing its trade creditors or to pay the salaries and wages due to its employees and there is no source of further obtaining such funding'.

Mr Potgieter submitted that this passage from Sacks' affidavit showed that Sacks was prepared to expedite a delivery of meat from Snyders of Rainbow early on a Monday morning while being well aware that the close corporation was not only in a parlour

situation but that a decision had already been taken at 4.30 p.m. on the preceding Friday to liquidate the corporation. In this he had manifestly been reckless.

Mr Hodes, who appeared together with Mr Sievers on behalf of defendant, began his argument by an examination of the manner in which plaintiffs had pleaded its case. The essence of this case, in Mr Hodes' view, was set out in the pleadings as being that between the 21 August 2000 until 15 September 2000 Sacks had ordered meat on behalf of Sacks Butchery. Thus 'Sacks, gedurende die periode vermeld…. namens Sacks Butchery tjeks uitgeskryf het ten gunste van Eerste Eiser terwyl hy geweet het dat die vermelde tjeks nie gehonoreer sou word nie.' Furthermore, the quantum was set in the pleadings in the amount of R588 696,18.

Mr Hodes submitted that there had been no proof that Sacks had run the business recklessly with the intent to defraud first and second plaintiff during the period as pleaded. In his view, there was no evidence as to the value of the meat so ordered in the amount of R588 696,18 to justify a claim in this amount. Even on the assumption that Sacks had been reckless, there was a possibility that a further dividend would be made available to creditors. In this connection Mr Hodes referred to the liquidator's report of 19 December 2000. In that report the liabilities of the close corporation were said to exceed the assets by R6 168 001. However amongst the liabilities was an amount of R11 244 190 which was described as comprising trade creditors, loan creditors, public for meat stamps and anticipated damages claims. Furthermore the liquidator had stated 'The

trade debtors of the close corporation have an outstanding face value of R3 607 145. As at 9 November 2000 an amount of R1 232 666,64 had been collected from such debtors. Collections are ongoing and it is anticipated that an excess of R3 000 000 will be collected from the debtors. In this eventuality there was sufficient to cover the secured claim of Standard Bank of South Africa Limited in the amount of R1 577 416,00 and the balance will accrue to the benefit of the general body of creditors'. Mr Hodes contended that, absent a more recent report from the liquidator, the plaintiff was obliged to wait until a further dividend was paid in order to be in the position properly to quantify its damages.

Section 64(1) of the Close Corporations Act.

Section 64 (1) of the Act provides that 'If it at any appears that any business of a corporation was or is being carried on recklessly, with gross negligence or with intent to defraud any person or for any fraudulent purpose, a Court may on the application of the Master, or any creditor, member or liquidator of the corporation declare that any person who was knowingly a party to the carrying on of the business in any such manner, shall be personally liable for all or any of such debts or other liabilities of the corporation as the Court may direct, and the Court may give such further orders as it considers proper for the purpose of giving effect to the declaration and enforcing that liability.

This section follows the wording of section 424 of the Companies Act 61 of 1973. Hence the manner in which courts have sought to interpret s 424 is of considerable

relevance to this dispute. However it is necessary to deal firstly with a judgment relied upon by plaintiffs.

In **L & P Plant Hire BK en Andere v Bosch en Andere** 2002 (2) SA 662 (SCA) at 677 J – 678 A **Brand AJA** (as he then was) described the purpose of section 64 thus:

'Wat skuldeisers betref is die bedoeling van art 64….immers nie om vir hulle mede hoof skuldenaars met die beslote korporasie te skep nie. Die bedoeling is om hulle te beskerm teen nadeel wat die roekelose of gronalatige bedryf van die beslote korporasie se sake vir hulle mag meebring'.

Brand AJA then offers this significant qualification to the scope of section 64 at 678 B

'So gesien moet art 64, wat skuldeisers betref, beperking uitgelê word om slegs betrekking te hê op 'n roekelose en 'gronalatige' bedryf van die beslote korporasie se besigheid wat 'n nadelige effek op die skuldeiser se vordering teen die beslote korporasie het. Waar die beslote korporasie ten spyte van die roekelose of gronalatige bedryf van sy besigheid steeds die skuldeiser se vordering kan ontmoet, kan die skuldeiser nie ingevolge art 64 ageer nie'.

Whereas in the **L & P Plant Hire** case, a suspicion that a close corporation was unable to pay a debt was considered to be insufficient to justify the application of section 64, Mr Potgieter submitted that, in the present case, the close corporation had been liquidated, at the time of liquidation its liabilities far exceeded its assets, and further that it was not

clear whether any significant dividend would be realised. Thus plaintiffs would be left only as concurrent creditors.

Mr Potgieter submitted further that the plaintiffs had duly elected to pursue the recovery of damages by way of an action in terms of section 64 of the Act. The mere fact that minor dividends had been received from the realisation of assets in the liquidation of the close corporation together with the possibility that some future dividend might be received did not preclude plaintiffs from seeking relief in terms of section 64 of the Act.

Evaluation

In examining whether a close corporation has conducted its business recklessly or with gross negligence, a court must examine the principles which are inherent in the Act within the context of the particular facts of the case. For this reason the key factors to be considered in this enquiry include the scope of the business of the close corporation, the role, function and powers of the persons whom it is sought to hold liable, the amount of the debts of the close corporation, the nature and scope of the close corporation's financial difficulties and its prospects of recovery and the extent to which the persons whom it is sought to be held liable in terms of section 64 have deviated from the standard of a reasonable person. See in this connection **T J Jonk BK h/a Bothaville Vleismark v Du Plessis NO en 'n Ander** 1998(1) SA 971 (O).

This particularised approach to the application of section 64(1) of the Act finds

explication in the following **dictum** of **Howie JA** (as he then was) in **Philotex (Pty) Ltd and Others v Snyman and Others** 1998(2) SA 138 (SCA) at 146 G-I.: 'Participation in business necessarily involves taking entrepreneurial risks but s 424 only penalises the subjection of third parties to risk where (apart from the case of fraudulent trading) it is grossly unreasonable. If, therefore, in a given case there is some ground for thinking the creditors will be paid but a reasonable businessman would nonetheless, because of circumstances creating material but not high risk of non payment, refrain from running that risk, the director who does run that risk by incurring credit, and thus falls short of the standard of conduct of a reasonable businessman, trades unreasonably and therefore negligently **vis-à-vis** creditors. That departure from a reasonable standard could not clearly be described as gross, however and the director concerned would not be hit by the section. By contrast, an instance that manifestly would fall foul of this section is where a reasonable businessman would realise that in all the circumstances payment would not be made when due. To incur credit in that situation would, as a matter of degree be so plainly more serious a departure from the required standard than the conduct in the first example that one has no difficulty characterising it as grossly unreasonable and therefore grossly negligent….So, if a plaintiff were to present evidence warranting a conclusion that when credit was incurred there was, objectively regarded, a very strong chance, falling short of a virtual certainty, that creditors would not be paid, that case would, I think, also involve the mischief which the section was intended to combat'.

In the present case, the evidence of Ahlers confirms that the close corporation was a business which ran for many years with cash flow problems. Ahlers' own evidence was that, from time to time, he would receive a phone call requesting that a post-dated cheque be held back. In an affidavit deposed to by Sacks pursuant to the aborted application of plaintiff (upon which Mr Potgieter placed considerable reliance), Sacks stated: 'The cheques were not met as a result of the cash flow problem. To the knowledge of the Applicants the Butchery had suffered similar cash flow problems in the past and was doing so at the time that the cheques were handed over. I had no reason to believe that they would not be met'.

According to the liquidator's report, at the time of the liquidation, an amount of R3 607 145 was outstanding and significantly within a month of the close corporation being liquidated (namely as at 9 November 2000) an amount of R1 232 666,64 had been collected from debtors indicating that there were funds available for the discharge of certain liabilities including those of plaintiff.

In short, Mr Hodes submitted that, in the circumstances, the manner in which the business had been conducted over a long period of time and in terms of which Ahlers was aware, a reasonable businessman in the position of Sacks would not have realised that 'in all circumstances payment would not be made when due'. By contrast, the procedure adopted by Sacks accorded with a long standing practice. Notwithstanding the financial difficulties of the close corporation, a significant amount was owed by debtors who were

not recalcitrant in discharging their obligations as the record of collection by the liquidator revealed. Thus, Sacks had a rational basis upon which to expect that debtors would pay so that cash would be available to honour the cheques.

In seeking to rebut this approach, Mr Potgieter cited a **dictum** of **Van Deventer J** in **Ozinsky NO v Lloyd and Others** 1992 (3) SA 396 (c) at 414 G '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'.

Whatever inference can legitimately be drawn from the evidence, the test remains whether a reasonable business person standing in the shoes of Mr Sacks would run a business for a long time in circumstances where clearly there had been cash flow problems, which fact he had continued to communicate to his creditors.

The only evidence which raises a question as to compliance with this test is to be found in the evidence of Mr Snyders who was employed by Rainbow and not by plaintiffs. He claimed that Sacks still persisted with a meat delivery on Monday 18 September 2000, the day of the urgent application for liquidation of the close corporation. Given his vagueness about all dates other than these critical ones, there is, on this evidence alone, a somewhat unsatisfactory and inadequate basis for finding that Sacks' conduct fell within

the scope of section 64(1) of the Act as opposed to constituting acts which stand to be classified as falling just outside of the border of the scope of section 64(1) of the Act. Further, Snyders' evidence is not strictly relevant to the period in which it is alleged on the pleadings that a breach of s 64(1) took place.

There is a further and significant difficulty in the way of plaintiffs' success. While Mr Potgieter might be correct in saying that there was nothing in the papers to suggest that the plaintiff would obtain a further significant dividend, that possibility cannot be excluded on the basis of the figures provided in the liquidator's report together with the additional uncertainty as to the contingent liability owing to Lloyds insurance. In the liquidator's report the following statement appears: 'From the information made available to me from his trustee and dependent upon the negotiations for the release of certain securities which had been put up for obligations to Lloyds of London and Standard Bank, it would appear that an amount in excess of R1 000 000 may well become available as a dividend in respect of the close corporation's claim'.

In summary, plaintiff has not provided any evidence by way of a further report from the liquidator which would show that, on the probabilities, a further dividend of some considerable significance would not be paid out. To the contrary, there would appear to be a real possibility of a further dividend being paid to creditors. Accordingly, on the pleadings and hence on the specific case brought by plaintiffs, the latter have failed to prove, on the probabilities, as to what loss may have suffered by it even were it to prove

that the conduct of Sacks fell within the scope of section 64(1) of the Act or that a fraudulent misrepresentation had been made by Sacks.

For this reason Mr Potgieter was constrained to ask for a declarator, being that the estate of Sacks is declared to be personally liable to the first plaintiff in terms of the provisions of Section 64(1) of the Act in the amount of R588 696,18 less any dividends that the first plaintiff may receive in respect of its claim in Sacks & Son CC (in liquidation); further that the estate of Sacks is declared to be personally liable to the second plaintiff in terms of the provisions of Section 64(1) of the Act in the amount of R63 918,70, less any dividends that the second plaintiff may receive in respect of its claim in the close corporation.

As Mr Hodes correctly submitted, both causes of action relied upon by plaintiff have to fail in that plaintiff has failed to prove the **quantum** of any claim. In both claims, plaintiffs claim damages where no basis for the quantification of damages has been established. Further, Ahlers confirmed in evidence that a dividend had been received by plaintiff from the close corporation in liquidation, thereby reducing plaintiffs'claims for goods sold and delivered.

Mr Ahlers was also referred to a letter of the trustee of 21 August 2002 which stated 'please note that I do not anticipate that there will be any further account lodged in this matter until most probably June 2004 as it is only at that stage that we would have

established whether or not any funds are going to revert to the insolvent estate from his Lloyds' investments and whether or not there will be funds to distribute to his creditors'. He was then asked 'In ander woorde hoeveel U uiteindelik gaan kry uit Sacks & Son CC weet u nie, is dit reg so?' To which he replied 'Ek weet nie niemand weet nie Edel Agbaar'.

To the extent that the provisions of section 64(1) confer a discretion upon this court, that discretion, in my view, cannot be exercised in favour of plaintiffs who might in future be in receipt of substantial dividends in addition to those already received. In this connection, an exercise of this discretion in favour of plaintiff would run the risk of mulcting the creditors of Sacks' insolvent estate of dividends to which they would otherwise be entitled.

For all these reasons, the action is dismissed with costs including those consequent upon the employment of two counsel.

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DAVIS J