

**To lift or not to lift the corporate veil – the unfinished story:  
A critical analysis of common law principles in  
lifting the corporate veil.**

**by**

**Louis Velaphi Mthembu  
B.A.,LL.B. (Natal)**

**The dissertation is submitted in partial fulfilment of the requirements for the Degree of Master of Laws, by coursework, Faculty of Law, University of Natal.**

**(2002)**

## TABLE OF CONTENTS

Preface.....	x
Declaration .....	xi
Acknowledgement .....	xii
1. Introduction.....	1
2. Legal personality.....	8
2.1 Introduction.....	8
2.2 Concept of corporate personality.....	8
2.3 The legal nature of corporate personality.....	9
2.3.1 Fiction theory.....	9
2.3.2 Concession theory.....	10
2.3.3 Realist theory.....	11
2.3.4 Juristic reality theory.....	11
2.4 The effect of incorporation.....	12
2.4.1 Suing and being sued.....	12
2.4.2 Perpetual succession.....	13
2.4.3 Power to own property.....	13
2.4.4 Protection of the members from liability.....	14
3. The company as a legal distinct person.....	15
3.1 Introduction.....	15
4. General overview of common law principles in piercing the corporate veil..	23
5. The English approach to piercing the corporate veil.....	27
5.1 Introduction.....	27
5.2 Fraud or improper conduct.....	29

5.2.1	The motive of the fraudulent person.....	33
5.2.2	The character of the legal obligation being evaded.....	34
5.2.3	The timing of the incorporation of the device company.....	34
5.3	Evasion of legal obligations.....	35
5.4	Agency or alter ego.....	36
5.5	Just and equitable exception.....	39
5.6	Enemy character.....	40
5.7	Summary.....	42
6.	The South African approach to piercing the veil of corporate personality.....	43
6.1	Introduction.....	43
6.2	Perpetration of fraud.....	44
6.3	The Lategan rule.....	46
6.4	Unconscionable injustice.....	50
6.5	The balancing test.....	54
6.6	Economy rationale principle.....	56
6.7	Summary.....	57
7.	Cape Pacific decision and post 1995.....	59
7.1	Introduction.....	59
7.2	The trial court approach.....	61
7.3	The balancing approach followed by the Appellate Division.....	62
7.4	Conclusion.....	70
8.1	General Summary.....	73
8.2	Conclusion.....	77
	Bibliography.....	78

Table of cases.....	81
Table of statutes.....	85

## Preface

Let it at once be said that this work in no way lays claim to being an exhaustive analysis of the company law in South Africa. At best, then, it may be described as a survey of South African company law. The emphasis is on principle rather than detail.

The scope of the research is broad. There is really no significant aspect of company law, which directors are not concerned. In a sense, my work is one on company law seen through a director's eyes.

I have tried to cater for interested layman by whatever possible, expressing myself in simple and non-technical language.

LV MTHEMBU

## **Declaration**

I hereby declare that this research is entirely my own work.

## **Acknowledgement**

My dissertation is dedicated to my mother who has provided tremendous support and who has been pillars of strength to me.

This study would not have been possible without the kindness and assistance given to me by a large number of people. In particular, I wish to thank Nii Ngubane for the deep interest she took in the progress of my research.

I am especially grateful to Tshepho Mongalo for his invaluable comments on the different drafts of this study, and the considerable kindness he has shown to me.

To my supervisor, Christopher Schembri, I owe a special debt of gratitude, not only for innumerable personal kindness, but also for his constant encouragement and enthusiasm. He has been a mentor and a great inspiration to me.

# CHAPTER 1

## INTRODUCTION

The need to create an artificial legal person arises with the development of commercial enterprises involving large numbers of contributors of risk capital. A corporation is thus a legal device normally adopted to establish a business enterprise as an independent entity.<sup>1</sup>

In any established legal system there arises a need to create artificial legal entities having the capacity of acquiring rights and incurring obligations to a great extent as human beings.

However, the term "incorporation" should be confined to those occasions where the legal system declares that it is creating a new legal entity and endowing it with the standard corporate attributes of perpetual succession, the ability to own the property required for the conduct of its business and capable in law of suing and being sued.

The recognition by the law that a corporation is a legal entity distinct from its members is often described as the veil of incorporation. A corporate veil falls between the corporation as a separate entity and its members in such a way that it hides them from the view of outsiders looking at the corporation.

---

<sup>1</sup> HA Ford, *Principles of Company Law*, 2ed. 1978 at 2

In many instances courts have preserved the inviolability of the corporate veil.<sup>2</sup> This is because once a corporation is duly incorporated, the courts usually do not look behind the veil to inquire why the corporation was formed or who really controls the corporation. This is clearly illustrated by a number of both English and South African cases<sup>3</sup>. The corporate personality seems to be an important encouragement for the entrepreneurial activities in so far as the members are concerned.<sup>4</sup>

By itself however, corporate personality may be subject to abuse, hence courts may in some instances refuse to recognise the existence of a separate personality of the entity or it may examine who really controls the corporation.

This process is usually described as piercing the corporate veil.<sup>5</sup> The effect of piercing the veil is either to render other persons usually members or directors jointly liable with the corporation for its obligations or to identify them with the corporation as a single person.<sup>6</sup> Piercing the corporate veil seems to permit courts to ignore the separate existence of the legal personality.<sup>7</sup>

---

<sup>2</sup> H Sher, *Piercing the Corporate Veil*, (1994) 4 Part 2 JBL at 51

<sup>3</sup> See below at 28

<sup>4</sup> For example wrongs committed by a corporation's directors, officers and employees, or by its agents within the scope of their authority, are chargeable to the corporation and not to its members.

<sup>5</sup> Or lifting the corporate veil

<sup>6</sup> JM Gullick, *Ranking & Spicers' Company Law* 12ed. (1981) at 8

<sup>7</sup> See below at 4

It should be noted that piercing the corporate veil may be invoked by virtue of legislation or where no provisions of the legislation authorising the lifting of the corporate veil, the courts may do so in terms of common law principles.<sup>8</sup>

The doctrine of piercing the corporate veil is an important and powerful weapon in combating or at least deterring the abuse of the separate personality of a corporation by its members, directors, officers or employees and its agents.

It should be noted however, that piercing the corporate veil is an exceptional procedure and therefore, special or exceptional circumstances must exist before the court could pierce the veil.<sup>9</sup> The general rule is that the corporate entity should be recognised and upheld except in the most unusual circumstances.<sup>10</sup>

The courts have failed to formulate a single, coherent principle under which the corporate veil may be pierced in terms of common law principles. Hence it is very difficult to predict the circumstances in which the corporate veil will be lifted in the absence of a specific legislation so directing.

---

<sup>8</sup> RC Williams, *Concise Corporate and Partnership Law*, 2ed (1997) at 100.

<sup>9</sup> *Cape Pacific Limited v Lubner Controlling Investments (Pty) Limited* 1993 (2) SA 784 (C) 819 - 821.

<sup>10</sup> *Lee v Lee's Air Farming Limited* 1961 AC 12; 1960 3 ALL ER 420 (PC).

It has been said that the reported cases in which judges have lifted the veil in terms of common law principles are inconsistent, haphazard and irrational and that it is consequently difficult to predict, in any given situation, whether or not a court will lift the veil.<sup>11</sup>

Courts seem to give different general formulations as to when the corporate veil will be lifted in terms of common law principles. Thus, courts have tended to rely on a number of separate, unrelated categories of conduct as grounds for piercing the corporate veil.<sup>12</sup>

For example, courts are prepared to disregard the existence of the corporate entity in cases of "fraud" or "improper conduct",<sup>13</sup> or where a company has been used to "evade legal obligations",<sup>14</sup> or where a company is said to have been the "agent" or, perhaps more accurately, the "alter ego" or "instrumentality", of its controlling shareholders or where it does not in truth, carry on its own business or affairs, but acts merely in the furtherance of the business or affairs of its shareholders. In other words,

---

<sup>11</sup> Williams *op cit.* at 100

<sup>12</sup> A. Domanski, *Piercing the Corporate Veil - A New Direction* (1986) 103 SALJ at 224

<sup>13</sup> *R v Gillette* 1929 AD 364, *Food & Nutritional Products Limited v Neuman* 1986 (3) SA 464 (W), *Pressma Services (Pty) Limited v Schuttler* 1990 (2) SA 411 (C) 415, *Shipping Corporation of India Limited v Evdomen Corporation* 1994 SA 550 (A), *Cape Pacific v Lubner Controlling Investments Limited* 1995 (4) SA 790 (A), *Le Bergo Fashions CC v Lee* 1998 (2) SA 608 (C), *Re Darby Ex Parte Brougham* [1911] 1 KB 95

<sup>14</sup> See *Gilford Motor Co Limited v Horne* [1933] Ch 935, *Jones & Another v Lipman & another* [1962] WLR 832, *Botha v Van Niekerk en ander* 1983 (3) SA 513 (W)

where its controllers do not treat it as a separate entity carrying on business to promote its stated objects.<sup>15</sup>

It should be noted that the list of the categories of situations the courts have lifted the veil is by no means exhaustive. This state of affairs is not wholly satisfactory because the categories sometimes overlap and many do not articulate the principles on which they were decided.<sup>16</sup> The categorising approach hardly gives one any concrete idea about which conduct does or does not trigger the piercing of the corporate veil doctrine.

It is against this background that common law approaches in lifting the veil must be examined. The purpose of this research is an examination of South African law, in which some United Kingdom reported decisions on key issues are considered. The research seeks to demonstrate how the lack of a single, coherent principle has brought an element of inconsistency and uncertainty into the law.

Chapter 2 of this research merely examines the concept of the corporate personality in order to afford an understanding of the concept itself. The theories on the legal nature of the corporate entity will also be considered in this chapter.

Chapter 3 examines the position of a company as a separate entity distinct from its members. It will be argued that the judgement of *Salomon v A Salomon & Co Ltd*<sup>17</sup> is primarily associated with the salutary company-law principle that a company even if closely held, is a legal entity distinct from its members.

---

<sup>15</sup> See *Smith, Stone & Knight Ltd v Birmingham Corp* 1939 4 All ER 116, See also *Robinson v Randfontein Estate Gold Mining Ltd* 1921 AD 168-194

<sup>16</sup> See RC Williams op cit. 100

<sup>17</sup> [1897] AC 22 (HL)

Chapter 4 is the general overview of common law principles in lifting the corporate veil. Chapter 5 examines the English judicial approach to piercing the corporate veil. It will be argued that English courts have almost relied invariably on a number of discrete, unrelated categories of conduct upon which to base decisions to disregard the corporate personality of a company,<sup>18</sup> but this approach in the end is unsatisfactory.

In Chapter 6, the position in South Africa will be canvassed. It will be argued that the common law approach in piercing the corporate veil prior to the judgement of **Cape Pacific (Pty) Ltd v Lubner Controlling Investments (Pty) Ltd**<sup>19</sup> exemplifies the judicial adherence to a categorising approach, for the purpose of piercing the veil. This state of affairs is almost similar to their English counterparts.

In Chapter 7, it will be suggested that in a recent judgement of the **Cape Pacific v Lubner Controlling Investments (Pty) Ltd**,<sup>20</sup> there is to be found a broad, unifying principle which could serve as a basis for deciding piercing cases in a more logical and judicially satisfactory manner. It will be argued that the judgement of Cape Pacific represents a move away from the categorising approach towards a balancing of the need to preserve the separate corporate existence against the policy considerations justifying piercing the corporate veil (the balancing approach).<sup>21</sup>

---

<sup>18</sup> See A Domanski, *Piercing the corporate veil- A new direction* (1986) SALJ AT 224.

<sup>19</sup> 1995 (4) SA 790 (A)

<sup>20</sup> Supra

<sup>21</sup> The Appellate Division in Cape Pacific Ltd case held per Smalberger JA, concurred in by Vivier JA, FII Grosskopf JA, and Van den Heever JA, that courts should not lightly disregard a company's separate personality, but should strive to give effect to and uphold it, but where fraud, dishonesty or other considerations proved to exist, the court will justifiably disregard the corporate personality (802H-804A). The need to preserve the separate

The discussion is summarised in Chapter 8, where the suggestion is made that as regard veil piercing, courts can learn from the American jurisprudence. It will be argued that the balancing approach should be followed in South Africa. The balancing approach at least attempts to weigh up considerations that are relevant to the inquiry (piercing the corporate veil).

---

corporate identity would in such circumstances have to be balanced against policy considerations which arise in favour of piercing the corporate veil and a court would then be entitled to look to substance rather than form in order to arrive at the true facts, and if there has been a misuse of a corporate personality to disregard it and attribute liability where it should rightly lie. Domanski correctly submits that a categorising of instances where the courts may be willing to pierce corporate veil may lead to a too strict approach, especially in those instances where there has been no abuse of the corporate entity and the company itself is desirous that the veil should be pierced. He fully supports an approach based on principles and policy consideration i.e. balancing test identified and applied in *Glazer v Commission on Ethics for Public Employees* 431 So 2d 752 (LA 1983).

## CHAPTER 2

### 2.1 INTRODUCTION

It has been accepted that in any established legal system there arises a need to create artificial legal entities, which are capable of acquiring rights, and incurring legal obligations in much the same way as human beings.<sup>22</sup>

The concept of corporate personality will be discussed briefly in this chapter in order to achieve a better understanding of the concept itself. The theories of corporate personality will also be discussed in order to shed some light on the legal nature of the corporate personality.

### 2.2 Concept of corporate personality.

A corporation is a person in the legal sense of the word. The expression 'legal person'<sup>23</sup> means an entity capable of having legal rights and incurring legal obligations.<sup>24</sup> This means legal personality is not a natural phenomenon but a creature of law.<sup>25</sup>

Thus, the law determines which entities or objects may be accorded legal personality. A company and certain other bodies or associations are "juristic" persons,<sup>26</sup> and therefore, enjoy the status of separate legal personality.

---

<sup>22</sup> See above page at 1

<sup>23</sup> Latin; persona

<sup>24</sup> RC Williams, *Concise Corporate and Partnership Law* 2ed (1997) 73

<sup>25</sup> JH Beale, *Conflict of Laws* II 120.2

<sup>26</sup> By contrast a human being is a natural person.

## 2.3 THE LEGAL NATURE OF CORPORATE PERSONALITY

There have been a number of divergent theories formulated on the nature of legal personality. But, not one of these theories on the legal nature of legal personality can be said to be completely satisfactory.<sup>27</sup>

Wolf,<sup>28</sup> identifies four of these theories. He holds the view that these theories, namely the "fiction theory", "concession theory", "realistic theory" and "jurists' reality" theory, should be given serious attention.<sup>29</sup>

### 2.3.1 Fiction Theory

In terms of the fiction theory, only human beings can be regarded as persons and therefore capable of acquiring rights and incurring legal obligations.<sup>30</sup> In contrast to human beings, corporations are endowed with this capacity by law.

In a nutshell a corporation is regarded as a fictitious entity, which has no physical existence at all. Cilliers makes a reference to the case of Sutton's Hospital,<sup>31</sup> where the court stated that [a corporation aggregate of many is invisible and vest only in intendment and consideration of the law].<sup>32</sup>

---

<sup>27</sup> See HS Cilliers, *Corporate Law* (1977) 3eds at 4--5

<sup>28</sup> "The Nature of Legal Person" (1938) *Law Quarterly Review* at 496

<sup>29</sup> See also Van Wyk S, *Corporate Personality & A Comparative Overview of the Judicial Disregarding of Corporate Veil* (1992) at 10

<sup>30</sup> Cilliers & Benade, *Company Law* (1984) 4ed at 8

<sup>31</sup> 1612 10 C Rep 1A 32 B,

<sup>32</sup> The theory was also referred with approval by the court in *Universiteit van Pretoria v Tommie*

The fiction theory was also referred with approval by the court in the judgement of *Gumede v Bandhla Vukani Bakhithi Limited*,<sup>33</sup> where Charlisle J. considered that a company possesses a legal persona, which is apart from its members.<sup>34</sup> Thus, a company has neither body nor passion. It cannot be loyal or disloyal, neither can it possess any characteristics belong to a race. It should be noted that the moral significance of the theory is that it asserts, and attempts to guarantee, individual moral autonomy.<sup>35</sup>

### 2.3.2 Concession Theory

This theory is closely related to the fiction theory. In terms of this theory, the grant of legal personality is a concession by the state. Thus, it is inherent in this concession that the legal person can never be empowered to function in conflict with the legal order.<sup>36</sup>

This theory purports to explain that the memorandum and articles of association of a company are interpreted almost like a creative statute and thus very strictly.<sup>37</sup>

---

*Meyer Films 1979 (1) SA 441 (A) at 458*

<sup>33</sup> 1950 (4) SA 560 (N)

<sup>34</sup> At 561

<sup>35</sup> WA Joubert, *The Law of South Africa (LAWSA)* (1995) Vol.4 Part 1 at 31

<sup>36</sup> Cilliers op cit. note 5 at 3

<sup>37</sup> Cilliers op cit. at 5

### 2.3.3 Realistic Theory

In terms of the realistic theory a legal person is a physical reality, which in essence reveals the same characteristic as a natural person and therefore must be treated and judged in the same way.<sup>38</sup> Thus, the recognition of corporate personality is no different in principle from the recognition of the legal personality of natural persons.<sup>39</sup>

### 2.3.4 Juristic reality theory.

This theory is similar to the realistic theory. It suffices to mention that this theory is viewed by many academics as the most acceptable and satisfactory approach.<sup>40</sup> It purports to explain the nature of legal personality with regard to any underlying assumptions about the nature of social life. Thus, in truth, legal personality is a legal concept and as such it is always artificial, and at most, it is a "juristic person".<sup>41</sup>

---

<sup>38</sup> Cilliers op cit. at 5

<sup>39</sup> Joubert op cit. at 31

<sup>40</sup> Cilliers op cit. at 6

<sup>41</sup> Joubert op cit. at 32

## 2.4 THE EFFECT OF INCORPORATION

On its formation, a corporation, as an independent entity becomes endowed with rights and obligations. This means that a corporation acquires its own legal personality and existence apart from its members. Numerous practical consequences flow logically from the fact that a corporation exists apart from its members.<sup>42</sup>

### 2.4.1 Suing and being sued

Because a corporation is a separate legal entity, it follows that it may enforce rights by suing and conversely it may incur liabilities and be sued by others. Thus, one of the practical consequences of incorporation is that a corporation can sue and be sued in its own name. It follows that where any wrong is done to a corporation; it is the proper person to take legal action to enforce its rights.

At common law, the ability of individual members to enforce wrongs done to their company is severely limited by the rule in *Foss v Harbottle*,<sup>43</sup> which requires the company itself to be the person enforcing its rights. Therefore, in order to redress a wrong done to the company or to recover moneys or damages alleged to be due to the company, the company should prima facie bring the action itself.<sup>44</sup>

---

<sup>42</sup> Cilliers op cit. at 6

<sup>43</sup> [1843] 2 Hare 461, 67 ER 189

<sup>44</sup> At 192, for example in *Caxton (Pty) Ltd v Reeva Forman Ltd* 1990 (3) SA 547 (A) at 560 H-L, the court held that a trading company has a right to sue for damages in respect of a defamatory statement, which is calculated to injure its business reputation, also in *Dhlomo NO v Natal newspapers (Pty) Ltd* 1989 (1) SA 945 AT 948G-953G, the court considered that a company may claim damages to compensate it as a result of the defamation. The court in *Motors Industry Fund Administrators Ltd v Janit* 1994 (3) SA 56 (W) AT 60H-J referred with approval to the

### 2.4.2 Perpetual succession

The corporation continues to exist despite changes in its membership. The law therefore, provides for what is called perpetual succession. In *Maasdorp & Another v Harddow NO & Another*,<sup>45</sup> the court considered that a change in the membership of the shareholders would not ordinarily affect the legal rights of a corporation and to its immovable property, for it would remain vested with the ownership and would continue in possession and occupation thereof.<sup>46</sup>

In a nutshell all that would be changed would be the control of the corporation. It follows that the existence of the corporation will not be affected by the death of a member. Even if all members of a corporation were killed, the corporation would still survive.

### 2.4.3 Power to own property

Another obvious consequence of the fact that a corporation is a separate legal entity is that it may own property distinct from the property of its members. This means that members do not have the proprietary interest in the property of the company.<sup>47</sup> Thus, in *Shipping Corporation of India Limited v Evdom Corp*<sup>48</sup> the court stated that it was

---

judgement of *Financial Mail (Pty) Ltd v Sage Holdings Ltd* 1993 (2) SA 452 (A) as authority to the fact that a company has a right to privacy.

<sup>45</sup> 1959 (3) SA 861 ( C )

<sup>46</sup> At 866

<sup>47</sup> See *Macaura v Northern Assurance Company Ltd* [1925] AC 619

<sup>48</sup> 1994 (1) SA 550 (A)

important to keep distinct the property rights of a company and those of its shareholders, even if the latter is a sole member.<sup>49</sup>

#### **2.4.4 Protection of the members from liability**

A major reason for forming a company in many instances is that the shareholders wish to limit their liability should the business proposed to be carried on by the company incur losses.<sup>50</sup> In certain circumstances, however the members of a company may be held liable for what appears to be legal obligations of the company.

---

<sup>49</sup> At 560

<sup>50</sup> Cilliers op cit. at 14

## CHAPTER 3

### THE COMPANY AS A LEGAL DISTINCT PERSON

#### 3.1 Introduction

Our law recognises that on incorporation of a company, it acquires an independent legal personality and exists apart from its members. As such the company acquires its own rights and incurs its own legal obligations. This means that corporate obligations vest in the company and not the shareholders, directors and employees of such entity.

The incorporation of a company gives rise to the so-called corporate veil. The corporate veil falls between the company as a separate entity and its members in such a way that it hides them from the view of outsiders looking at the company.

The principle that a company is legal person separate from its members has its origin in common law.<sup>51</sup> In the leading judgement of *Salomon v Salomon & Company Limited*<sup>52</sup> the court formulated the principle that a company is a legal person in its own right, separate from its members and directors. It follows that the members and directors of a company are not liable per se for the company's debts.

In this case Salomon promoted a company, which was duly registered and incorporated according to law (Joint Stock Act). He sold his business to the company he floated. Instead of receiving cash, as consideration, he was allotted certain shares in the company and debentures to secure the balance of the purchase price. The only

---

<sup>51</sup> JB Cilliers, SM Luitz, *The Corporate Veil, Unnecessary Confining Corset?* (1996) 56 THRHR at 523

<sup>52</sup> [1897] AC 22 (HL)

other shares issued were six in number and were allotted to six members of Salomon's family.

The company failed and in the winding-up the question arose as to whether Salomon's debentures were preferential to the claims of other creditors. It was contended on behalf of other creditors that Salomon and the company was one and the same person, in view of his shareholding and that consequently the company's debts were really his debts.<sup>53</sup> In the circumstances, they asked the court to lift the corporate veil in order to render Salomon personally liable for what appeared to be the company's obligations.

However, the House of Lords held that any consideration of the composition of the members of the company was irrelevant and that, once incorporated, the company must be treated as an independent person in the eyes of the law.<sup>54</sup> On appeal the House of Lords held:<sup>55</sup>

"...the company is at law a different person altogether from the subscribers to the memorandum and that though it may be that after incorporation the business is precisely the same as it was before incorporation, and the same persons are managers, and the same had received the profits, the company is not in law the agent of the subscribers or trustee for them. Nor are the subscribers as members liable in any shape or form, except to the extent and in the manner provided by the Act...Any member of a company acting in good faith is much entitled to take and hold the company's debentures as any outside creditor"

The quoted passage vividly demonstrates that trading in the form of a company with its own legal personality is legally permissible. This means that the company would be recognised as a legal person even where members of the same family held all its

---

<sup>53</sup> At 24

<sup>54</sup> At 48

<sup>55</sup> At 51-2

shares. This applies even where only one person is effectively controlling all the shares in a company.

The major significance of this decision is that the veil of incorporation was not lifted and the privilege of corporate personality accorded, even when on the facts of the case, ownership and control of the corporate entity were entirely in the hands of Salomon himself.<sup>56</sup> The decision also shows that to interfere with the corporate personality is a delicate exercise.

Gower remarks that Salomon's case is a decision, which opened up new vistas to company lawyers and the world of commerce.<sup>57</sup> Thus, not only did it finally establish the legality of the 'one man company and showed that the incorporation was readily available to the small private partnership and sole trade as to the large public company, but also revealed that it was possible for a trader not merely to limit his liability to the money which he puts into the enterprise, but even to avoid any serious risk to the major part of that by subscribing for secured debentures rather than shares.<sup>58</sup>

He remarks further that the result seems shocking and the decision has been much criticised. The only justification for it is that the public deals with a limited company at their own peril and knows or ought to know what to expect. Thus, a trader, by forming a company to carry on his business, could legally avoid personal liability for the debts of the business. Although such avoidance may seem to be unfair, members of the public

---

<sup>56</sup> LSS Seally, *Corporate Personality in the 20<sup>th</sup> Century* (1995) 58 Cambridge Law Journal at 247

<sup>57</sup> *Principles of Modern Company Law* (1976) 6ed. at 612

<sup>58</sup> At 612

who deal with limited liability companies know or ought to know<sup>59</sup> the legal implication of doing so.

Hertzberg points out that the effect of the decision in Salomon's case is to make it possible for sole traders and partners to form and conduct their business with limited liability.<sup>60</sup> The controllers of such entity can further protect themselves by becoming secured creditors of the company. This enables them to rank ahead of unsecured creditors in the event the company is wound up.<sup>61</sup>

The decision in Salomon's case is significant, as it was not until the House of Lords handed down its decision that a company was fully recognised as being a separate legal entity. This recognition was applied in a different context in **Macuara v Northern Assurance Company Limited**<sup>62</sup>. The appellant, the owner of a timber estate, assigned the whole of the timber to a company called Irish Canadian SawMills Limited. The company paid a full purchase price to the appellant for the timber.

The company then proceeded with the cutting of the timber. The applicant subsequently became the creditor of the company for a certain amount of cash. The appellant had insured the timber estate against fire by policies effected in his own name. The timber was destroyed by fire and the appellant claimed compensation from the insurance company. The insurance company repudiated the claim on the ground that the appellant had no insurable interest in the timber.

---

<sup>59</sup> Members are presumed to know because the company's articles of association and memorandum of association are public documents.

<sup>60</sup> *Understanding Company Law* (1986) 2ed. at 21

<sup>61</sup> Hertzberg op cit. at 22

<sup>62</sup> [1925] AC 619 HL

The court upheld the contention by the insurance company. It held that the timber belonged to the Irish Canadian SawMills Limited of Skibberrean Company Cork and not to the appellant.<sup>63</sup> The court held further that it was of cardinal importance to keep distinct the property rights of a company and those of its shareholders.<sup>64</sup>

The court held further that although the appellant owned almost all the shares in the company in question, and the company owed him a good deal of money, neither as a creditor nor as shareholder, could the appellant insure the company's assets.<sup>65</sup>

The recognition that a company is a legal person was also applied in a different context in Lee v Lee's Air Farming Limited.<sup>66</sup> Lee in carrying on his business of aerial top-dressing had formed a company of which he beneficially owned all the shares and was a sole governing director of the company.

Pursuant to the company's statutory obligations he caused the company to insure against liability to pay compensation under the Workmen's Compensation Act. He was killed in a flying accident. The company employed Lee as a chief pilot. His wife sued the company for compensation, claiming that at the time of his death, her husband was a "worker" employed by the company.<sup>67</sup>

---

<sup>63</sup> At 624

<sup>64</sup> At 625

<sup>65</sup> At 625

<sup>66</sup> [1961] AC 12

<sup>67</sup> At 13

The Court of Appeal held that his widow was not entitled to compensation from the company (the company's insurers) since Lee could not be regarded as a 'worker' within the meaning of the Act.<sup>68</sup>

However, the Privy Council reversed the decision. It held that Lee and his company were distinct legal entities, which had entered into contractual relationships under which he became the chief pilot, a servant of the company.

The fact that the deceased was a controller and governing director in one company did not mean that he could not be its employee in another (as a pilot). This flowed from the independent personality of the company. The company and the deceased were separate legal persons.<sup>69</sup>

With regard to the question of dual capacities, the court commented that it is well established in the law that a person can possess and function in dual capacities, and citing as authority the judgement of ***Fowler v Commercial Timber***.<sup>70</sup> Thus, in effect the magic of corporate personality enabled him to be a master and servant at the same time and to get all the advantages of both and of limited liability.<sup>71</sup>

---

<sup>68</sup> At 18

<sup>69</sup> At 30

<sup>70</sup> [1930] 2KB 1 at 20

<sup>71</sup> The decision in *Lee v Lee's Air Farming* shows that in the context of company law, the same person may wear two hats, that is to say that act in different capacities in the affairs of the company.

The principle that a company has a distinct legal personality is further illustrated in the leading South African case of **Dadoo (Pty) Limited v Krugersdorp Municipal Council**,<sup>72</sup> where in terms of a statute of the South African Republic<sup>73</sup> the person mentioned<sup>74</sup> were prohibited from owning immovable property in the Transvaal, but nothing was mentioned as to Asiatic Companies.

On 12 February 1915 a company called Dadoo Limited was registered at Pretoria with a share capital of 15 000.00 pounds divided into 150 shares of 100 pounds each. Mahomed Dadoo owned 149 shares and one share was owned by one Dindar, who were both Indians. In March 1915 Dadoo Limited bought and took transfer of a stand in the township of Krugersdorp. This stand was subsequently let to Dadoo in his individual capacity, who carried on a grocery and general dealer's business on it.

The Krugersdorp Municipal Council applied to the Transvaal Provincial Division for an order setting aside the transfer for as being a contravention of Laws 3 of 1885. Innes CJ on appeal, delivering the majority judgement said the following:<sup>75</sup>

"I come to inquire whether ownership the transaction complained of is a contravention of the statute. Thus whether ownership by Dadoo Limited is in substance ownership by its Asiatic shareholder. Clearly in law it is not. A registered company is a legal person distinct from its members who compose it... Nor is the position affected by the circumstances that a single member may hold a controlling interest in the concern. This conception of the existence of a company as a separate entity from its shareholders is not merely artificial and technical thing. It is a matter of substance; property vested in the company is not and cannot be regarded as vested in all or any of its members."

---

<sup>72</sup> 1920 AD 530 [6]

<sup>73</sup> Law 3 of 1885

<sup>74</sup> I.e. The races of Asia

<sup>75</sup> At 550-1

The court held therefore, that the statutory prohibition did not apply to companies even though Asiatics held their shares. Clearly the court in Dadoo's case upheld the inviolability of corporate personality.<sup>76</sup>

---

<sup>76</sup> See also *Gumede v Bandhla Vukani Bakhathini Ltd* 1950 (4) SA 60 (N) at 72.

## CHAPTER 4

### A GENERAL OVERVIEW OF COMMON LAW PRINCIPLES IN PIERCING THE CORPORATE VEIL.

#### 4.1 Introduction

Even though a company is a separate legal person, members can in a wide variety of circumstances become personally liable for what appears to be acts, liabilities and obligations of the corporation. Thus, in certain instances the courts are prepared to peer through the corporate veil to give effect to the facade of a company or even to ignore the separate existence of the legal person.

This is often described as piercing the corporate veil (or lifting the corporate veil).<sup>77</sup> The doctrine of piercing the corporate veil asserts that in certain circumstances a court is empowered to disregard the principle of the separate legal existence of a company.

However, when the court thus pierces the corporate veil, it does so for the purpose of adjudging the rights and liabilities of the parties in the matter before it. This means that disregard of the corporation's existence is confined to the particular case.<sup>78</sup> For all other purposes the company's separate existence remains unaffected.<sup>79</sup>

---

<sup>77</sup> These two concepts will be used interchangeably in this research.

<sup>78</sup> See *DHN Food Distributors Ltd v London Borough of Tower Hamlets* 1976 3 All ER 462, 467, 1976 1 WLR 852 (CA) 860, where the court pierced the corporate veil and consequently considered that a group of three companies for the present purpose be treated as one. Even when a corporate veil is pierced in a particular context, the corporation will still be recognised as valid under other circumstances.

<sup>79</sup> See Joubert *op cit.* at 77

The court often pierces the corporate veil in an attempt to prevent abuse of corporate personality by members, directors, employees and agents of a company. The court either ignores the company or treats its members as if they were the owners of its assets and were conducting its business in their personal capacities.<sup>80</sup>

It is accepted that if the corporate personality has been used as a device to cover "fraud" or for "improper conduct",<sup>81</sup> or where it has been used as an "agent" or "alter ego",<sup>82</sup> or if it is "just and equitable",<sup>83</sup> to do so, the court will pierce the corporate veil,<sup>84</sup> and attribute personal liability to those misusing the principle of corporate veil.<sup>85</sup>

However, it is disappointing that courts have still not laid down a more coherent principle under which the corporate veil should be lifted at common law. It has been said that the reported cases, in which courts have lifted the veil in terms of common law

---

<sup>80</sup> Larkin MP, (1989) SALJ at 387

<sup>81</sup> See e.g. *Cape Pacific (Pty) Ltd v Lubner Controlling (Pty) Ltd* 1995 (94) SA 790 (A), *Gilford Motor Co v Horne* 1933 Ch 945 (CA), *Jones v Lipman* 1962 WLR 832, *Re Darby* 1911 1 KB 95, *Lategan v Boyes* 1980 (4) SA 191 (T), *Botha v Van Niekerk* 1983 (3) SA 513 (W), *Re a Company* 1985 BCLC 33 (CA), *The Shipping Corp of India Ltd v Evdomon Corp* 1994 (1) SA 550 (A) 566, *Re Bugle Press Ltd* 1961 Ch 270 (CA), *Cattle-breeders Farm Ltd v Veldman* 1974 (1) SA 169 (RAD)

<sup>82</sup> See *Smith, Stone & Knight Ltd v Birmingham Corp* 1939 4 All ER 116, *DHN Food Distributors Ltd v London Borrow of Tower Hamlets* 1976 1976 3 All ER 462, 1976 1 WLR 852 (CA), *Briggs v James Hardie Ltd* 1989 16 NSWLR 549, *Ritz Hotel v Charles of the Ritz Ltd* 1988 (3) SA 290 (A).

<sup>83</sup> See *In Re Yenidje Tobacco Ltd* 1916 2 Ch 426 (CA)

<sup>84</sup> H Sher, *Piercing the Corporate Veil* (1996) 4 Part 2 JBL AT 51

<sup>85</sup> Gibson, SA Mercantile & Company Law (1997) at 269

principles, are inconsistent, haphazard and irrational and that it is consequently difficult to predict, in any given situation, whether or not a court will lift the veil.<sup>86</sup>

This state of affairs can be observed not only in South Africa, but also in England. Thus, both in England and South Africa, courts have failed to formulate a single coherent principle upon which decisions to disregard the juristic personality is based.<sup>87</sup>

The lack of a general test can be attributed to the fact that courts have relied invariably on divergent and unrelated categories (such as "fraud" or "improper conduct", "agency" or "alter ego", "evasion of legal obligations", "abuse of the corporate form") to decide whether the corporate veil should be lifted.<sup>88</sup> This list is by no means exhaustive.

Williams<sup>89</sup> correctly submits that this state of affairs is not wholly satisfactory as the categories sometimes overlap and many do not articulate the principle on which they were decided. It is the writer's submission that the common law principles hardly give one any idea about which conduct does or does not trigger the piercing of the corporate veil doctrine.

---

<sup>86</sup> See Domanski *op cit.* at 224

<sup>87</sup> LC Davids, *'The lingering question: Some perspective on the lifting of the corporate veil'* (1994) TSAR at 155

<sup>88</sup> See A. Domanski, *Piercing the Corporate Veil - A New Direction* (1986) 103 SALJ at 224.

It is submitted that this list is no by means exhaustive.

<sup>89</sup> *Concise Corporate and Partnership Law* 2ed (1997) at 100

It is against this background that common law approaches in piercing the veil must be examined. The topic of piercing the veil of corporate personality must be looked at in a historical perspective. Hence the issue will be addressed in the manner proposed above.<sup>90</sup>

---

<sup>90</sup> See page 5

## CHAPTER 5

### THE ENGLISH APPROACH TO PIERCING THE VEIL OF CORPORATE PERSONALITY.

#### 5.1 Introduction

The principle so firmly established in Salomon's case<sup>91</sup> that a company is a legal person entirely separate and distinct from its members, must be contrasted with the line of cases relating to piercing the veil of corporate personality.<sup>92</sup>

There are several English cases where the issue of piercing or lifting the corporate veil in terms of common law principles has been dealt with. However, it should be noted that the English courts have in most instances relied on a categorising approach in lifting the corporate veil. They have lifted the corporate veil where it is convenient to do so. The writer submits that this state of affairs is not satisfactory because the lack of a single

---

<sup>91</sup> *Supra*

<sup>92</sup> There has been a great deal of discussion as to the correct word to use in order to describe the process of bypassing the Salomon principle, see for example S Ottelenghi 'From Peeping behind the Corporate Veil to ignoring it completely' (1990) 3 M.L.R. 338, Staughton L.J. in *Atlas Maritime Co. SA V Avalon Maritime Ltd (No. 1)* [1991] 4 ALL E.R 769, 779 stated that to pierce the corporate veil is an expression which means treating the rights or liabilities of its shareholders as that of a company. To lift the corporate veil or look behind it on the other hand should mean to have regard to the shareholders in a company for some legal purpose [original emphasis]. For the purpose of this research the phrase 'lifting the veil' or "piercing the veil" will be used interchangeably.

coherent principle makes it difficult to predict when the court will lift or not lift the corporate veil.

Gower,<sup>93</sup> writing in the context of the English law, submits that instances of piercing the corporate veil reveal no consistent principle beyond a refusal by the legislature and the judiciary to apply the principle laid down in Salomon's case.<sup>94</sup>

Domanski<sup>95</sup> argues that until recently the courts in England, United States and South Africa alike have failed to formulate a single, coherent principle upon which to base decisions to disregard the separate juristic personality of a company.<sup>96</sup> Thus, judges have almost relied on one or other of a number of discrete, unrelated categories of conduct in order to justify such decisions.

English courts in particular have identified and applied a number of categories (exceptions)<sup>97</sup> to the principle enunciated in Salomon's case. These categories (exceptions), namely "enemy character", "just and equitable" doctrine; "agency" or "alter ego", "fraud" or "improper conduct", "evasion of legal obligations" will be discussed in this chapter.

---

<sup>93</sup> *Modern Company Law* (1979) 4ed

<sup>94</sup> At 103

<sup>95</sup> *Piercing the Corporate Veil - A New Direction?* (1986) 103 SALJ at 224

<sup>96</sup> At 224

<sup>97</sup> The terms will be used interchangeably in this research.

## 5.2 Fraud or improper conduct.

Fraud can be identified as the most commonly proposed exception to the separate entity principle.<sup>98</sup> There are several English cases, which have applied the principle that the court will disregard the corporate personality in cases of "fraud" or "improper conduct". Thus, if the corporate personality has been used for the purpose of fraud or as a device to cover fraud or to evade contractual or other legal obligations or improper conduct, courts will pierce the corporate veil.

This principle is often described as the "fraud exception" to the Salomon principle.<sup>99</sup> Farrar<sup>100</sup> points out that the courts are prepared to pierce the corporate veil in order to combat fraud. Thus, courts will not allow the principle of corporate personality to be used as an engine to commit fraud. For an example in **Re Darby, Ex Parte Broughton**,<sup>101</sup> the court confirmed the principle that the court will pierce the corporate veil if a company is used to perpetrate any form of fraud.<sup>102</sup>

In this case Darby and another person formed a company in the Channel Islands, with themselves as the only directors and sole shareholders along with other five others as their nominees. The company then formed and registered another company in Wales and sold to it a quarrying licence and certain plant at a vast overvalue. When the company went into liquidation, the liquidator claimed from Darby the secret profit made by him out of the promotion of the Welsh Company.

---

<sup>98</sup> See *Salomon v Salomon & Co* [1897] AC 22 (HL)

<sup>99</sup> P Jennifer, *Lifting the Corporate Veil: A Reassessment of the Fraud Exception* (1997) 56 Cambridge Law Journal at 284

<sup>100</sup> *Farrar's Company Law* (1991) 3d at 75

<sup>101</sup> [1911] 1 KB 95

The court held that it was Darby who was the real promoter of the Welsh Company, the Channel Island company being only the vehicle for the perpetration of a fraud.<sup>103</sup> In the circumstances, the court lifted the corporate veil in respect of the latter company.

This case illustrates the firm approach by courts that any personal profit, made using the mechanism of the corporate form, where there is a conflict of duties and interest, may equally be deemed improperly made and the corporate form may be disregarded by the court.<sup>104</sup>

The other two classic examples of the fraud exception are Gilford Motor Co. Ltd v Horne<sup>105</sup> and Lipman v Jones.<sup>106</sup> The former judgement concerns an attempted use of corporate personality to effect the breach of a covenant clause in the form of a restraint of trade agreement.

The Court of Appeal clearly considered that Mr Horne formed the company as a "device" or a "stratagem" and a "mere cloak or sham" in order to mask the effective carrying on of business by him.<sup>107</sup> In other words the company was formed to enable Horne to continue to breach the agreement. Based on the aforesaid, the court lifted the

---

<sup>102</sup> At 103

<sup>103</sup> At 103

<sup>104</sup> See HL French, *Case Book on Australian Corporation Law* (1991) 5ed at 12. See also *Adams v Cape Industries* supra at 1026, where it was assumed that a court will pierce the corporate veil where a defendant by device of a corporate structure attempts to evade limitations imposed on his conduct by the law.

<sup>105</sup> [1933] Ch 935 (CA)

<sup>106</sup> [1962] WLR 832

<sup>107</sup> Per Lord Hanworth M.R. at 936

corporate veil by granting an order restraining both the former employee and the company from competing with the plaintiff.

Concurring with the majority judgement, Lawrence L.J. confirmed<sup>108</sup> that the defendant company was a "channel" used by Mr Horne for the benefit to obtain the advantages of the customers of the plaintiff and that therefore the defendant company ought to be restrained together with Mr Horne.<sup>109</sup>

In the judgement of *Lipman v Jones*,<sup>110</sup> the first defendant had agreed to sell freehold land with registered title to the plaintiff for certain amount. The defendant sold and transferred the land to the defendant company, which he acquired and in which he became the shareholder and the director with another person.

The court specifically referred to the judgement of *Gilford Motor Ltd v Horne*,<sup>111</sup> and held that the company was a "mask", which Mr Lipman held before his face in an attempt to avoid recognition by the eye of equity.<sup>112</sup> Accordingly, the court lifted the corporate veil against both the defendants.

The writer submits that the same result could have been achieved without lifting the veil in this case. Williams<sup>113</sup> correctly argues that the court could simply have made an order that Lipman did all things within his power to pass transfer of the property to Jones and that he controlled the company therefore, it was within his power to ensure

---

<sup>108</sup> At 119 H-I

<sup>109</sup> At 119H-I

<sup>110</sup> Supra

<sup>111</sup> Supra

<sup>112</sup> At 836

<sup>113</sup> Concise Corporate and Partnership Law op cit. at 103

that transfer was passed to Jones.<sup>114</sup> Alternatively the court could have granted an interdict, restraining defendants from trading in competition with the plaintiff (Jones).

For an example in *Genwest Batteries (Pty) Ltd v Van der Heerden*<sup>115</sup> the court, preferring not to grapple with the doctrine of lifting the corporate veil, and holding instead that companies controlled by the persons subject to the restraint agreement, granted an interdict restraining those companies from trading in competition with the applicant.<sup>116</sup> Based on the aforementioned decision, the writer submits that lifting the corporate veil was not appropriate in Lipman's case.

Nevertheless, what is significant about these cases is that a court will pierce the corporate veil where a defendant by device of a corporate structure attempts to evade limitations imposed on his conduct by the law.<sup>117</sup>

This means that where a company is a sham or is merely used for the purpose of doing something for a person that that person is himself forbidden by the law to do, the court may disregard the separate existence of the company and treat the acts of the company as the acts of the person concerned. The two cases have been characterised as involving the abuse of corporate form.<sup>118</sup>

Larkin<sup>119</sup> submits that a "mere cloak or sham", "device" and a "mask" are favourite terms of abuse in the well-known overseas cases,<sup>120</sup> which are said to amount to

---

<sup>114</sup> See *Cape Pacific (Pty) Ltd v Lubner Controlling Investments (Pty) Ltd* (supra)

<sup>115</sup> 1991 (1) SA 727 (T)

<sup>116</sup> See at 728-729

<sup>117</sup> See also *Adams v Cape Industries plc* 1990 Ch 433 544; 1991 1 All ER 929 (Ch & CA) at 1026

<sup>118</sup> See J Pyne, *Lifting the corporate veil*: 1997) Cambridge Law Journal at 285

<sup>119</sup> Pyne op cit. at 284

examples of piercing the veil.<sup>121</sup> Larkin further submits that the difficulty lies in the application of these terms because it is difficult to recognise a sham company.

The writer submits that it is only in exceptional circumstances that an argument based on the fraud will succeed because of the enormous burden placed upon the plaintiff to establish the impropriety of the activities involved. It seems that for the fraud principle to be successfully invoked the following aspects need to be established first:<sup>122</sup>

### 5.2.1 The motive of the fraudulent person.

With regard to this aspect, an element of deception is necessary. For example, in Hilton v Plustile<sup>123</sup> the Court of Appeal held that the plaintiff was not entitled to lift the corporate veil since he had full knowledge of the facts at all material times.

In Adams v Cape Industries,<sup>124</sup> considering whether the corporate personality had been used in such a way to justify the corporate veil being lifted, the court held that the test in relation to a company was whether the company had been used as a 'mere façade' concealing the true facts.<sup>125</sup> Applying this test to the facts before it, the court held that the proven motive of the perpetrator might be highly relevant.<sup>126</sup>

---

<sup>120</sup> See e.g. *Gilford Motor Co v Horne* supra at 961 and *Jones v Lipman*, supra at 836

<sup>121</sup> See also *Robinson v Randfontein Estate Gold Mining Co Ltd* 1921 AD 168 AT 194

<sup>122</sup> See J Pyne, *Lifting the corporate veil: A reassessment of the fraud exception* (1997) Cambridge Law Journal at 286.

<sup>123</sup> [1989] 1 WLR 149

<sup>124</sup> [1990] Ch 433

<sup>125</sup> At 542

<sup>126</sup> At 543

In the decision of Gilford Motor Co Ltd v Horne,<sup>127</sup> it became apparent that a company was set up for the very purpose of avoiding a restraint of trade agreement entered into by a former employee of the plaintiffs. The court granted rightly an order restraining both the former employee and the company from trading in competition with the plaintiff.<sup>128</sup>

### **5.2.2 The character of the legal obligation being evaded.**

Pyne submits<sup>129</sup> that for the fraud exception to succeed, the defendant must intend to deny the plaintiff a pre-existing legal right. Thus, if no pre-existing right is present, any intention on the part of the defendant to deceive the plaintiff must be of a speculative and accordingly less substantial in nature.

### **5.2.3 The timing of the incorporation of the device company.**

It is submitted that it should be irrelevant that a device company is an existing, solid entity with its own business, as long as it has been used as a tool to effect the fraud, the court will lift the corporate veil.<sup>130</sup>

The ratio in *Gilford Motor*<sup>131</sup> and *Jones*<sup>132</sup> is that the separate legal personality of a company will not be upheld if the company has been used as a device to allow another (whether a company or an individual) to evade its existing obligations.

---

<sup>127</sup> Supra.

<sup>128</sup> The court in *Adams v Cape Industries*, supra confirmed the principle that a court will pierce the corporate veil where a defendant by the device of a corporate veil structure attempts to evade such rights of the relief against him as the third party already possesses.

<sup>129</sup> At 288

<sup>130</sup> Pyne op cit. 289

Based on the aforesaid requirements, it seems that the fraud exception places a heavy burden on the part of the plaintiff to establish all the elements mentioned above.

Nevertheless, the fraud exception seems to be mostly favoured by courts. For instance in the judgement of the Re Bugle Press Ltd.,<sup>133</sup> the use of a company as a device to cover fraud was refused by the court. In this case there were three shareholders and two wanted to buy out the third shareholder, who refused. Subsequently, the majority shareholders formed a company to make an offer for all of the shares in order to comply with the law.

The Court of Appeal, looking to substance rather than form, disregarded the existence of a company and therefore held that the company was a "mere sham" or "simulacrum".<sup>134</sup>

### **5.3 Evasion of legal obligations**

This exception can also be identified as the most commonly proposed exception to the separate entity principle and allows the court to lift the corporate veil. This exception applies for example, where a company is a sham, merely used for the purpose to do something for a person that that person is himself forbidden by law to do. The court may ignore the separate existence of the company and treat the acts of a company as the acts of the person concerned.<sup>135</sup>

---

<sup>131</sup> Supra

<sup>132</sup> Supra

<sup>133</sup> [1961] Ch 270, (CA)

<sup>134</sup> At 289

<sup>135</sup> See *Adams v Cape Industries*, supra at 1026, where it was assumed that a court will pierce the

In the context of South African law, the decision of Cattle-breeders Farm (Pty) Ltd v Veldman,<sup>136</sup> clearly confirms the above-mentioned principle. In this case a company of which Veldman was the sole shareholder and the managing directors claimed the ejection of Veldman's wife from a house on the farm leased to the company. The house had been the matrimonial home before Veldman left after committing adultery. He had not offered his wife any alternative accommodation.

The court correctly held that the company was nothing more than Veldman's "*alter ego*" and accordingly refused to allow him to avoid his matrimonial duties and obligations.<sup>137</sup> In the circumstances, the court regarded Veldman and the company as one person.

#### 5.4 Agency or alter ego

It is accepted that a court will lift the corporate veil in the circumstances where the company may be regarded as the mere agent or instrument of the controlling shareholder. For example, in Re A Company,<sup>138</sup> the Court of Appeal pierced the corporate veil and granted an order restricting companies controlled by the defendant, where evidence showed that the defendant had formed a corporate network (subsidiary companies) to dispose of his assets.<sup>139</sup>

---

corporate veil where a corporate structure attempts to evade such rights of relief against the Defendant as a third party already possesses.

<sup>136</sup> 1974 (1) SA 169 RAD

<sup>137</sup> At 173

<sup>138</sup> [1985] BCLC 333 (CA)

<sup>139</sup> At 342

Therefore, in the context of veil piercing, the term "agency" is used to describe a situation where a company is said to have been the agent or the "alter ego" or "instrument" of its controlling shareholders. Thus, where the company does not in truth, carry on its own business or affairs, but acts merely in the furtherance of the business or affairs of its controlling shareholders the court will lift the corporate veil.<sup>140</sup>

It should be noted however, that the doctrine of piercing the corporate veil has often been confused in academic writings and in judicial pronouncements with law of agency.<sup>141</sup> It is not entirely clear whether the characterisation of the company as the "alter ego" of the controlling shareholders indicates that the court is using an agency test.

It is accepted that in order for the holding company to be held liable for the debts of its subsidiary under the law of agency, the general principles of the law of agency need to be applied to the facts of the particular case.<sup>142</sup> For example, the court in the decision of **Smith, Stone & Knight v Birmingham Corp**,<sup>143</sup> the court in applying the agency test correctly looked upon two companies as one economic unit.<sup>144</sup>

The court held that it was a question of fact in each case, whether a holding company is acting as agent for its subsidiary company and thus, if there is an agency the controlling company will be liable for the acts of its subsidiary.<sup>145</sup> Hence the court

---

<sup>140</sup> See Joubert op cit. at 90

<sup>141</sup> See D Milo, *The liability of a holding company for the debts of its subsidiary: Is Salomon still alive and well* (1998) South African Law Journal at 326

<sup>142</sup> Milo op cit. at 326

<sup>143</sup> [1939] 4 All ER 116

<sup>144</sup> At 122

<sup>145</sup> At 123

described the subsidiary company as the "agent" or "employee" or "tool" or "simulacrum" of the holding company.<sup>146</sup>

The *DHN Food Distributors Ltd v London Borough of Tower Hamlets*<sup>147</sup> is also a case where the holding company was held to be entitled to compensation for disturbance where the property owned by its subsidiary, but on which the holding company carried on business was unlawfully acquired.<sup>148</sup>

A number of "trade mark" cases have also engaged agency jurisprudence.<sup>149</sup> For an example in *Ritz Hotel v Charles of the Ritz Ltd & Another*,<sup>150</sup> the question was whether the holding company had acted as the agent of its wholly owned subsidiary. The court held that agency had been established, though not in the legal sense, however in the sense that the holding company was acting on behalf of subsidiary company.<sup>151</sup>

It is clear from these decisions<sup>152</sup> that in order for the holding company to be held liable for the obligations of its subsidiary company under the law of agency, the general principles of the law of agency need to be applied to the facts of the particular case.<sup>153</sup>

<sup>146</sup> In this case the defendant acquired property occupied by the wholly owned subsidiary of the Plaintiff. The parent company, in order to succeed in an action for compensation for loss, had to establish that the subsidiary was its agent.

<sup>147</sup> [1979] 3 All ER 462, [1976] (1) WLR 852 (CA)

<sup>148</sup> At 472

<sup>149</sup> See *Milo* op cit. at 327

<sup>150</sup> 1988 (3) SA 290 (A)

<sup>151</sup> At 317B: The court held that agency could be inferred on the facts because of a "request either express or tacit, by the [subsidiary] to the [holding company], see *Milo* op cit. note 60 at 327

<sup>152</sup> *Smith, Stone & Knight Ltd v Birmingham Corp*, *DHN Food Distributors Ltd v London Borough*

However, in the context of veil piercing, one is not entirely sure if the characterisation of the companies as "agent" or "alter ego" of the controlling shareholders, that the court is applying agency test (the general principles) based on the law of agency. Thus, the court does not seem to articulate the principle on which the alter ego doctrine is founded in so far as companies and shareholders relationship is concerned.

### 5.5 Just and equitable exception

This category can also be identified as the most commonly used to disregard the separate existence of the corporation.<sup>154</sup> For an example, in the event of an underlying partnership, the intention between parties may be recognised by the courts even though the parties formed a company to carry their intention into effect.<sup>155</sup>

In **Re Yenidje Tobacco Co Ltd**,<sup>156</sup> W and R who traded separately as tobacco and cigarette manufacturers, concluded an agreement to merge their businesses and in order to achieve this, formed a company. They became the shareholders and directors of the said company. But, differences arose between W and R, which led to the deadlock in management of the business.

The court accordingly held that it was just and equitable that a winding-up order should be made.<sup>157</sup> The court held that although W & R were carrying on the business by

---

*of Tower Hamlets and Ritz Hotel v Charles of the Ritz Ltd, supra*

<sup>153</sup> See Milo op cit. at 326

<sup>154</sup> Van Wyk op cit. 36

<sup>155</sup> See *Bellars v Hodnett* 1978 (1) SA 1109 (A), *Moosa v Mavjee Bhawan (Pty) Ltd* 1966 (4) SA 462 (T)

<sup>156</sup> [1916] 2 Ch 426 (CA)

means of the machinery of a limited company, however in substance they were partners.<sup>158</sup> This means that if this had been an ordinary partnership and an action had been brought for dissolution, the plaintiff, who was the petitioner in this case would have been successful, as there would have been sufficient ground for dissolution of partnership.

The courts in determining whether a company should be wound up on the grounds of the "*just and equitable*" doctrine had taken the personal relationship between the shareholders into account.<sup>159</sup>

## 5.6 Enemy character

In classifying a company as an enemy in the time of war, a court may pierce the veil of incorporation and look at the character of its directors and shareholders. The judgement of **Daimler Co Ltd v Continental Tyre & Rubber Co (GB) Ltd**<sup>160</sup> offers an example where the personal characters of the shareholders and directors were imported to the company.<sup>161</sup>

---

<sup>158</sup> At 429

<sup>159</sup> See *Lawrence v Lawrich Motors (Pty) Ltd* 1948 (2) SA 1029 (W); See also Van Wyk op cit. 36.

<sup>160</sup> [1916] 2 AC 307

<sup>161</sup> The question in this case was whether payment of a company registered in England, whose shares save for one, were held by Germans and whose directors were all Germans and resident in Germany, would be payment to an enemy and so illegal. The court stated that the question of control was a very important factor in determining whether a company could bear an enemy character and determining such control.

Lord Parker accepted that a company could assume an enemy character if those *in de facto* control are enemies or taking instructions from or acting under the control of enemies<sup>162</sup>.

It should be noted however that the court in *Dadoo (Pty) Ltd v Krugersdorp Municipal Council*<sup>163</sup> distinguished the Daimler decision. It considered that the difference between the two cases was that in Daimler the enquiry related to attributes, which in the nature of things could not be attached to a mere legal persona. The court in Daimler deemed it fit to look behind the company and to pay regard to the personality of the shareholders, who composed and control the entity.

In Dadoo on the other hand the question was whether the ownership of the company was in reality the ownership by the shareholders. The court maintained that a company and its shareholders were separate persons and accordingly refused to lift the corporate veil.<sup>164</sup> It is questionable as to whether the decision in Daimler could ever be reconciled with cases such as Dadoo.<sup>165</sup>

---

<sup>162</sup> See Larkin op cit. at 288

<sup>163</sup> Supra

<sup>164</sup> At 128, see also Larkin op cit. at 288

<sup>165</sup> Supra

## 5.7 Summary

To sum up, it has been demonstrated above that English courts have relied invariably on a categorising approach upon which to base decisions to disregard the corporate personality of a company.

It has been argued that the categories of the situation upon which to base decision to pierce the corporate veil are by no means exhaustive, though the dominant ones are fraud, evasion of legal obligations and agency.<sup>166</sup> It has been canvassed that a categorising of instances where the courts may be willing to pierce the corporate veil may lead to a narrow approach.<sup>167</sup>

It seems that there is no clear principle in this area of law. The courts would only pierce the corporate veil where it is convenient to do so especially if the facts of a particular case fall within the ambit of a particular category. The other major difficulty is that in some instances there is an overlap between certain categories.<sup>168</sup>

---

<sup>166</sup> Domanski op cit. at 225

<sup>167</sup> See Jones v Lipman supra

<sup>168</sup> See page 30 -34

## CHAPTER 6

### THE SOUTH AFRICAN APPROACH TO PIERCING THE VEIL OF CORPORATE PERSONALITY PRIOR TO THE 1995 CAPE PACIFIC DECISION.

#### 6.1 Introduction

It has been canvassed above that South African law recognises that on the incorporation, a company acquires an independent legal personality and exists apart from its members.<sup>169</sup> In certain circumstances, however, a court may justifiably disregard the separate personality of a company in order to fix liability elsewhere for what appears to be acts of the company.<sup>170</sup> This is often described as lifting or piercing the corporate veil.<sup>171</sup>

Until recently<sup>172</sup> South African courts have tended to follow their English counterparts in so far as piercing the corporate veil is concerned. They have chosen to rely on a

---

<sup>169</sup> See *Dadoo Co Ltd v Krugersdorp Municipal Council* supra at 550-1 where it was stated that a registered company is a legal persona distinct from the members who compose it... That result follows from the separate legal existence with which such corporations are by statute endowed, and the principle has been accepted in our practice. This conception of the existence of a company as a separate entity distinct from its shareholders is not merely artificial and technical thing. It is a matter of substance, property vested in the company is not and cannot be regarded as vested in all or any of its members.

<sup>170</sup> See *Sher* op cit. at 51

<sup>171</sup> See above at 5

<sup>172</sup> Prior to the judgement of *Cape Pacific (Pty) Ltd v Lubner Controlling Investments (Pty) Ltd* supra

number of discrete, unrelated categories of conduct upon which to base decisions in piercing the corporate veil.<sup>173</sup> However, the most dominant categories of conduct include fraud or improper conduct, abuse of the independent legal personality and evasion of legal obligations.

It will be contended that these categories in the end are unsatisfactory. Thus, a categorising of instances where the court may be willing to pierce the corporate veil may lead to a strict approach, especially in those circumstances where there have been no abuse of the corporate entity and the company itself is desirous that the veil should be pierced.<sup>174</sup>

## 6.2 Perpetration of fraud

As discussed above that South African courts have tended to follow their English counterparts in so far as piercing the veil of corporate personality in terms of common law principles is concerned. For example in R v Gillett,<sup>175</sup> the court refused to let the company be used to perpetrate fraud.<sup>176</sup> The court held that evidence showed that there had been a conspiracy on the part of the companies and Gillette to contravene the law for which they were liable in the absence of proof that they were not parties thereto.<sup>177</sup>

---

<sup>173</sup> Sher op cit. at 51

<sup>174</sup> See Domsaki op cit. at 224

<sup>175</sup> 1929 AD 364

<sup>176</sup> Gillette formed two companies, one, which provided loans, while he formed the other company to deal with loan applications. The former company charged the legal rates, while the latter charged a commission fee and renewal fees. Gillette was drawing all the profits from both companies.

<sup>177</sup> At 372

In the circumstances, the court held that Gillette, as the originator of the scheme was liable as a director and the sole shareholder of the companies, as he was the instigator of fraud.<sup>178</sup>

In another judgement of **Robinson v Randfontein Gold Mining Co Ltd**<sup>179</sup> the court refused to take into consideration the separate existence of a company where it was sought to use the subsidiary company as a device in evading a director's fiduciary duties to the holding company.<sup>180</sup>

Whilst the above-mentioned decisions demonstrate the willingness by courts to disregard the separate personality of a company and to fix liability to those who abuse or misuse the company to perpetrate fraud or for improper conduct, they do not represent a real support for a proper doctrine of veil piercing.<sup>181</sup>

The same is true in respect of the judgement of **Orkin Bros. Limited v Bell**,<sup>182</sup> where the directors allowed a company to buy goods on credit, knowing very well that a company would not be able to repay the debt.

---

<sup>178</sup> At 372-8

<sup>179</sup> 1921 AD 168

<sup>180</sup> At 194-195

<sup>181</sup> Larkin on *Piercing the Corporate Veil* (1989) SALJ at 235, argues that whilst South African decisions prior 1980s demonstrate the willingness of courts to disregard the principle of corporate personality as enunciated in *Salomon*, none of them represent real support for a proper doctrine of piercing the corporate veil.

<sup>182</sup> 1912 AD 198

The court held that fraud was being perpetrated on the seller and accordingly the court, for what appeared to be a debt of the company, held the directors of a company personally liable.<sup>183</sup>

McLennan<sup>184</sup> remarks that the decision has led to the theory that Orkin's decision is an example of lifting the corporate veil. McLennan refers to the judgement of Lategan NNO v Boyes,<sup>185</sup> where Le Roux J stated that the only true precedent for the principle (piercing the corporate veil) in our law is Orkin Bros Limited v Bell.<sup>186</sup>

McLennan holds the view that this approach cannot be correct.<sup>187</sup> Thus, in Orkin's case there was no question of lifting any veil, as there was no contractual privity and no fiduciary relationship between the agent (directors) and the third party (creditor).

Therefore, the only basis of liability in Orkin's case could have been in delict and the appropriate remedy was an award of damages.<sup>188</sup> Similar to the decisions in Gillett and Robinson, the court in Orkin's case did not make reference to the doctrine of piercing the veil of corporate personality.

---

<sup>183</sup> At 107

<sup>184</sup> The liability of Agents for Debts Contracted on behalf of Insolvent Companies (1998) South African Law Journal at 68

<sup>185</sup> 1980 (4) SA 191 (T)

<sup>186</sup> at 201 F-H

<sup>187</sup> McLennan op cit. at 68

### 6.3 Lategan rule

Larkin<sup>189</sup> argues that it was only the decade of the 1980's, which began with a quite explicit judicial affirmation of the piercing doctrine in South Africa. He supports his view by referring to the decision of Lategan NNO v Boyes,<sup>190</sup> where the defendant who was a director of a company signed a deed of suretyship in favour of the plaintiff.<sup>191</sup>

The defendant pleaded inter alia that he had signed the amended agreement only in his capacity as a director of the company, the principal debtor and not as surety. He contended that he had not, as a surety, consented to the amendment of the principal debt.<sup>192</sup>

The court considered the question whether in law it could be said that the second defendant had acted in both capacities when he had signed the amending agreement. The court said that the above issue raised the difficult question, whether and if so, when a court will pierce the corporate veil in order to ascribe knowledge or liability to someone in his personal capacity, where in point of fact he had acted only in a representative capacity.<sup>193</sup>

---

<sup>188</sup> McLennan op cit. 69

<sup>189</sup> Piercing the corporate veil (1989) South African Mercantile Law Journal at 276

<sup>190</sup> 1980 (4) SA 191 (T)

<sup>191</sup> The case involved an action for payment of the balance due in terms of the loan agreement, which was subsequently amended and signed by the second defendant on behalf of the company in favour of the plaintiff.

<sup>192</sup> At 192

<sup>193</sup> At 197

Le Roux J noted that the Canadian courts have refused to disregard the separate identity of companies except upon proof of fraud. He went on to state that he had no reason to believe that our own courts would go any further at the present juncture save where authorised by statute. He stated that:<sup>194</sup>

"I have no doubt that our courts would brush aside the veil of corporate identity time and again, where fraudulent use is made of the fiction of legal personality".

Applying this principle to the facts, the court conceded that the question whether in law it could be said that the second defendant had acted in both capacities when he had signed the amended agreement was a difficult one.<sup>195</sup>

Ironically, the court stated that the only true precedent for the principle in our law in supporting the proposition that the court would disregard the corporate identity where a company has been used to perpetrate fraud is the Orkin case.<sup>196</sup>

As discussed above<sup>197</sup> that although Orkin case seems to support the approach that proof of fraud or dishonesty may constitute the ground for disregarding the separate existence of a company, however the decision has nothing to do with the veil piercing doctrine.<sup>198</sup> It follows therefore, that the court's approach in Lategan' case was incorrect.

It should also be noted that in Lategan case, no question of fraud arose on the facts and the quoted passage that our courts would brush aside the veil of corporate identity

---

<sup>194</sup> At 198

<sup>195</sup> At 198-199

<sup>196</sup> At 201 H-F

<sup>197</sup> At page 45

<sup>198</sup> See criticisms of the judgement by J McLennan at page 45

time and again where fraudulent use is made of the fiction of legal personality, is obiter and not bidding.<sup>199</sup>

The decision in Letegan's case is characterised by the lack of analysis, as there was no actual application of the principle. The principle itself is unsatisfactory as it highlights a too strict approach, especially in those circumstances where there have been no abuses of the corporate entity.<sup>200</sup>

This could be attributed to the fact that fraud principle fails to take into consideration the fact that fraud may be a ground for lifting the corporate veil, but it is not the only ground. Thus, it is incorrect to assert that fraud is always an essential pre-requisite in such cases.<sup>201</sup> It seems that the court in Lategan case failed to recognise this and it failed to give a proper analysis under which the court could justifiably lift or pierce the corporate veil.

In a nutshell, Lategan case demonstrates the tendency of the courts to rely on categories for the purpose of piercing the corporate veil. It also highlights that reliance on categories of conduct upon which to base decisions to pierce the corporate veil may lead to a narrow approach, especially in those instances where there have been no fraud perpetrated by the members of the corporate entity.

---

<sup>199</sup> Domanski op cit. at 225, See also McLennan op cit. at 69

<sup>200</sup> See Lategan NNO v Boyes supra

<sup>201</sup> See e.g. *Botha v Van Niekerk en 'n ander 1983 (3) SA 513 (W)* at 519C-C, where Flemming J.

confirmed that fraud is not only ground upon which to base decision in piercing the corporate veil.

#### 6.4 Unconscionable injustice principle

In Botha v Van Niekerk<sup>202</sup> the court for once confronted the question of exactly what piercing the corporate veil actually means in the context of South African law.<sup>203</sup> The case concerned a contract of sale of a house, concluded on 24 September 1982. The purchaser was described in the contract as 'Van Niekerk'. The first respondent was the sole director and shareholder of the second respondent, the company.<sup>204</sup>

A guarantee for payment of the balance of the purchase price had to be furnished by 23 November. By 24 November the guarantee had not yet been given, and on that date the seller<sup>205</sup> addressed a demand to the first respondent in terms of the contract, which entitled the seller to cancel or to enforce the contract if the guarantee was not furnished within a further seven days.

Only on 29 November did the first respondent react by adopting the attitude that a nomination had taken place in terms of which the company had replaced him as purchaser. The company had been incorporated on 11 October 1982 with an authorised share capital of R1000.00, of which one R1 share had been issued.

The seller (applicant) chose to enforce the contract. The application was brought by him to enforce the contract. The applicant argued that the second respondent, company was merely the first respondent in another guise, and accordingly asked the court to pierce the corporate veil so as to enforce the contract of sale against the first

---

<sup>202</sup> 1983 (3) SA 513 (W)

<sup>203</sup> The fact of this case are very important in so far as to the principle is concerned.

<sup>204</sup> See Domanski op cit. at 226

<sup>205</sup> The applicant

respondent, regardless of the existence of the company and of any valid nomination that might have been established. The applicant also contended that the nomination was in any event nothing more than an attempt by the first respondent to evade his obligations in terms of the contract of sale.

The court held that on the facts there was no liability attached to the first respondent and that only the company was liable to the Applicant.<sup>206</sup> Fleming J. delivering the majority judgement formulated the test of "*unconscionable injustice*" for piercing the corporate veil, which he stated that.<sup>207</sup>

"...since limited liability is the crux of incorporation, it will at least require special grounds before this special characteristic is ignored, and that a court will only arrive at a finding of personal liability where the other party had suffered an unconscionable injustice as a consequence of something which, to a right-minded person, was clearly improper conduct on the part of the person who should be held liable, mere equity is not sufficient"

Thus, the first respondent could be held personally liable on the contract only if there were at least a conviction that the applicant had suffered '*unconscionable injustice*' as a result of what the right-minded person perceives to be clearly improper conduct on the part of the first respondent.

Applying this test to the facts, the court stated that there was no reason in equity or in law why the court should lift the corporate veil. The court further held that the company had not been used to perpetrate an '*unconscionable injustice*' and the seller had adequate legal protection.<sup>208</sup>

---

<sup>206</sup> At 525A-B

<sup>207</sup> At 523-525

<sup>208</sup> At 525-526

Williams<sup>209</sup> states three factors upon which the court based its judgement against the seller. Firstly, her institution of legal proceedings was premature because there was no proof that the company would not be able to pay the purchase price. The court held that although the company had no capital it might have been able to borrow money to pay the purchase price.<sup>210</sup>

Secondly, the seller was not at risk financially because performance and counter-performance under a contract must take place *pari passu*,<sup>211</sup> hence she was not obliged to pass transfer of the house to the purchaser unless and until she was paid the full purchase price.<sup>212</sup>

Lastly, if it later turned out that the purchaser's company was indeed unable to pay the purchase price, the seller would have a remedy under section 424 (1) of the Companies Act 1973 on the basis that the defendant had either fraudulently or recklessly, allowed the company to assume a debt which it could not pay. Under this section, the court could then declare van Niekerk personally liable for this debt.<sup>213</sup>

It is important to note that the court's enquiry in Botha's case led it to make a distinction between piercing the veil in the strict or true sense and something which falls short of this<sup>214</sup>.

Piercing the corporate veil in the strict sense or true sense involves rendering someone other than the company liable for its debts.<sup>215</sup> This of course requires a

---

<sup>209</sup> Concise Corporate & Partnership Law at 103

<sup>210</sup> At 526-527

<sup>211</sup> Simultaneously

<sup>212</sup> At 527

<sup>213</sup> See Domaski op cit. at 228

<sup>214</sup> At 521 -523

conviction that an unconscionable injustice had been suffered as a result of what the right-minded person regards as improper conduct.

The latter category on the other hand would include for instance the attribution of the personal qualities of the corporators to the company and statutory piercing of the corporate veil.

Larkin<sup>216</sup> expresses the view that true to the pattern, we still lack the true precedent for piercing the corporate veil, as the court in Botha did not see the facts there as calling for piercing the corporate veil. Implicit in the test propounded in Botha is the creation of a new piercing category, which is admittedly wider than mere fraud, but a category nevertheless.<sup>217</sup>

It is unfortunate that the court in Botha's case did not explain clearly what acts constitute improper conduct or what improper conducts would warrant a piercing of the corporate veil. The court offered no practical guidelines as to what constitute improper conduct in a particular case were given nor did it explain what unconscionable injustice mean.

The grounds upon which the court sought to justify its refusal to pierce the veil are not convincing. Domanski<sup>218</sup> expresses the view that the decision was harsh on the seller who had done everything that could reasonably have been expected of her in terms of the contract of sale.

---

<sup>215</sup> At 523

<sup>216</sup> (1989) SALJ at 279

<sup>217</sup> Domaski op cit. at 228

<sup>218</sup> Op cit. at 227

Furthermore, the conduct of the first respondent was clearly improper in that he had failed to comply timeously with his obligations in terms of the contract and also to exercise his right to appoint a nominee at a very late stage in the proceeding.

Thus, the timing and circumstances of the incorporation of the company appear to be suggestive of an intention on the part of the first respondent to evade his contractual obligations.<sup>219</sup>

The writer submits that considering the facts of the case and the test of an unconscionable injustice, the court in Botha would have been justified in piercing the corporate veil against the first respondent.

On the basis that the court did not see the facts as calling for piercing the corporate veil, it is submitted that the test formulated in Botha is obiter and does not lay down a judicial precedent for piercing the corporate veil.<sup>220</sup>

## 6.5 The balancing test

As regards veil -piercing, courts can learn from the American jurisprudence, which at least attempts to weigh up factors that are relevant to the enquiry.<sup>221</sup> The balancing test introduces flexibility into the law, and probably articulates what courts should do in piercing cases.

Domanski<sup>222</sup> refers to the American decision of Glazer v Commission on Ethic for Public Employees,<sup>223</sup> which he points out that the Louisiana Supreme Court

<sup>219</sup> See *Gilford Motors Co Ltd v Horne* and *Jones v Lipman*, supra

<sup>220</sup> Domanski op cit. at 228

<sup>221</sup> See Dario Milo, (1998) SALJ at 344.

<sup>222</sup> Domanski op cit. note 33 at 235

formulated a more coherent test (the balancing test) for piercing the corporate veil and that the test should be adopted in South Africa.<sup>224</sup>

In this case the question was whether the corporate veil should be lifted so that Glazer could be held personally liable for what appeared to be the conflict of interest by his wholly owned corporation.<sup>225</sup> The test for piercing the corporate veil was stated as follows:

[T]he policies behind recognition of a separate corporate existence must be balanced against the policies justifying piercing the corporate veil.

It seems that the balancing test requires an evaluation of competing policy considerations in order to determine whether or not the veil of incorporation should be disregarded.<sup>226</sup>

Until recently, the prevailing test for piercing the corporate veil in South Africa has been predominantly "fraud" or "improper conduct".<sup>227</sup> For example, in **Shipping Corporation of India Limited v Evidom Corporation**<sup>228</sup> the court expressed a conservative approach in relation to the circumstances justifying piercing the corporate veil. It held that the circumstances generally would have to include an element of "fraud" or "other

<sup>223</sup> 431 SO 29 [1983]

<sup>224</sup> See *Cape Pacific (Pty) Ltd v Lubner Controlling Investments (Pty) Ltd* supra

<sup>225</sup> Glazer was the sole shareholder and the chairman of the board of Glazer Steel Corporation, which supplied petroleum products to companies. The issue concerned the contravention of certain conflict of interest provisions of the Code of Ethics for Public Employees.

<sup>226</sup> The Appellate Division in *Cape Pacific (Pty) Ltd v Lubner Controlling Investments* applied with approval the balancing test. (see at page 56)

<sup>227</sup> Gibson, *SA Merc & Company Law* 7ed (1997) at 269, See also *Lategan NNO v Boyes*, supra

<sup>228</sup> 1994 (1) SA 550 (A)

improper conduct" in the establishment or use of the company or the conduct of its affairs.<sup>229</sup>

However, the court did not articulate its reasons for relying on the existence of fraud or other improper conduct in determining whether the separate legal existence of corporation should be disregarded. Nor did the court clarify what conduct would be regarded as constituting conduct which includes an element of fraud or improper conduct.

On the basis that the court in Shipping Corp failed to address the issues raised above, it is the writer's submission that the case affords little additional assistance to give pause to our criticisms of the common law approach in piercing the corporate veil. The case merely illustrates courts' adherence to a categorising approach in so far as piercing the corporate veil is concerned.<sup>230</sup>

## 6.6 Economic rationale principle

It should be noted however, that in the judgement of *Von Wuldfliq-Eybers & another v Sound-Props 2587 Investment CC*<sup>231</sup> the court pierced the corporate veil in the circumstances, which did not involve fraud or other improper conduct. In this case the plaintiffs had purchased the members' interest in a close corporation, the defendant which owned certain immovable property and effected certain improvements on the property of the Close Corporation.

Subsequently, it became clear between the parties that the agreement of sale was invalid. The plaintiffs instituted a claim for enrichment for the improvements that they

---

<sup>229</sup> At 566 E-F

<sup>230</sup> See also *Lategan v Boyes supra*.

<sup>231</sup> 1994 (4) SA 640 (C)

had effected to the property in their capacities as bona fide possessors, alternatively as bona fide occupiers.

The court held that the defendant had no economic rationale or business utility other than to avoid the payment of transfer duty.<sup>232</sup> In the circumstances, the court pierced the corporate veil.<sup>233</sup> It is the writer's submission that it is not entirely clear how the corporate veil was lifted in this case.

Furthermore, it is questionable whether the decision in Von Wulfflig-Eybers' case can be reconciled with decisions such as that in Dadoo's case, where the court refused to pierce the corporate veil, even though the company had no economic rationale<sup>234</sup>.

One is not entirely sure whether or not the court in Von Wulfflig-Eybers' case based its decision on the law of unjust enrichment. It is respectfully submitted that even in the context of the law of unjust enrichment, if the courts are to pierce the corporate veil on the ground that there is no '*economic rationale*' for the existence of the corporation, there is a danger of the concept of the separate legal personality of a company being significantly undermined if not destroyed.<sup>235</sup>

Nevertheless, the significance of Von Wulfflig-Eybers decision is that it demonstrates how the lack of a single, coherent principle has brought an element of inconsistency and uncertainty into the law in so far as piercing the corporate veil is concerned. This in fact coincides with the prevailing view that the law is far from settled with regard to the

---

<sup>232</sup> At 645 H-I

<sup>233</sup> At 645-648

<sup>234</sup> See also *Letegan NNO v Boyes*, *supra*

<sup>235</sup> See JJ Bolter, *Piercing the Corporate Veil* (1994) ASSA at 409

circumstances in which it would be permissible to pierce the corporate veil at common law.<sup>236</sup>

## 6.7 Summary

It has been argued that the tests propounded in *Lategan* and *Botha* are not bidding and therefore, do not add any value in terms of laying down a judicial precedent in so far as veil piercing is concerned.

It has also been argued that *Lategan's* case is precisely the kind of situation, which vividly exposes the inadequacy of the categorising approach. This conservative approach of the courts is apparently illustrated by the recent judgement of *Shipping Corp of India Ltd.*<sup>237</sup>

In a nutshell, the reported decisions discussed in this chapter illustrate the inconsistency of the courts in so far as lifting the corporate veil is concerned.

---

<sup>236</sup> See *Cape Pacific (Pty) Ltd v Lubner Controlling Investments (Pty) Ltd* at 803

<sup>237</sup> *Supra*

## CHAPTER 7

### CAPE PACIFIC DECISION AND POST 1995

#### 7.1 Introduction

The leading piercing case in South Africa is *Cape Pacific Ltd v Lubner Controlling Investment (Pty) Ltd*,<sup>237</sup> where the Appellate Division (Court of Appeal) stated that:<sup>238</sup>

...[T]he law is far from settled with regard to the circumstances in which it would be permissible to pierce the corporate veil. Each case involves a process of enquiring into the facts which once determined may be of decisive importance... Courts should not lightly disregard a company's separate personality, but should strive to give effect to and uphold it. But where fraud, dishonesty or other improper conduct is found to be present, other considerations will come into play. The need to preserve the separate corporate identity would in such circumstances have to be balanced against policy considerations which arise in favour of piercing the corporate veil."<sup>239</sup>

The facts of the case in Cape Pacific were complex and gave rise to assorted litigation.<sup>240</sup> They could be conveniently summarised as involving Lubner who owned shares in Findon Investment (Pty) Limited (Findon). The Findon shares were transferred to Lubner Controlling Investments (Pty) Limited (LCI) which held them on its behalf as a matter of convenience. LCI was owned by four trusts, created by Lubner's father for the benefit of Lubner's children through companies.

---

<sup>237</sup> 1995 (4) 790 (A)

<sup>238</sup> Per Smalberger JA, concurred in by Vivier JA, FH Groskopt JA, and Van der Heerden JA (dissented) and advocating a more conservative approach to piercing the corporate veil than that adopted by the majority. See also Milo, (1998) SALJ note 32 at 324.

<sup>239</sup> At 803. See also *Glazer v Commission on Ethics for Public Employees*, supra

<sup>240</sup> See *Sher* op cit. at 50

One of them, Gerald Lubner Family Trust (Pty) Limited (GLI) owned all shares in Lubner Controlling Investments (LCI), its sole director being S. In 1979 Lubner owned all the issued shares in GLI. It was clear on the facts that Lubner exercised complete control over LCI in respect of the Findon shares.

Cape Pacific successfully sued LCI for delivery of Findon shares, which LCI had sold in 1979 to Cape Pacific. At the trial, the court was of the view that Cape Pacific was entitled to those shares and therefore gave judgement in its favour. LCI appealed against the judgement of the trial court. But the Appellate Division dismissed the appeal with costs.

Subsequently, LCI failed to comply with the court order to deliver the shares to Cape Pacific. Cape Pacific brought an application against LCI and other parties to have them declared as being in contempt of court for failing to deliver the shares. However the application was not successful. Cape Pacific then sued Lubner, LCI and GLI for an order: -

- Compelling GLI to deliver the Findon shares to it or compelling GLI to deliver them to CLI and LCI then to deliver them to Cape Pacific;
- Compelling Lubner to cause GLI to deliver the shares to Cape Pacific; and
- Costs order against Lubner, GLI and LCI.

It was submitted on behalf of Cape Pacific that the court should pierce the corporate veil as the effective control of the companies, LCI and GLI had all times vested in Lubner and the purpose of the transfer of the shares in the company had been to defeat Cape Pacific's claim.<sup>241</sup>

---

<sup>241</sup> At 798

Williams<sup>242</sup> submits that the scenario is similar to a situation where, for example, a person sold the property, and regretting that he had done so and to avoid having to deliver the property to the purchaser, sold property again to a company which he controls. The latter company then claims that, as a separate legal persona, it is under no obligation to hand over the property to the first purchaser.

## 7.2 The trial court approach

Williams argues that in refusing to pierce the corporate veil, the trial court held that although the transfer of the shares could be described as improper, it had not resulted in an '*unconscionable injustice*' because the plaintiff had the opportunity to recover the Findon shares via a claim in terms of a contract, but had failed to use this remedy' and was therefore 'the author of its misfortune.'<sup>243</sup>

It seems that the decision of the trial court not to lift the veil was based on the two principles, namely: -

- The court will lift the veil only if there has been an unconscionable injustice.<sup>244</sup>
- The remedy of lifting the corporate veil is available only where the aggrieved party has no other legal remedy.<sup>245</sup>

---

<sup>242</sup> Concise Corporate and Partnership Law at 104

<sup>243</sup> Concise Corporate and Partnership Law at 104

<sup>244</sup> The principle formulated in *Botha v Van Nickerk*, *supra*

<sup>245</sup> At 805F.

### 7.3 Balancing approach adopted by the Appellate Division.

Subsequently, Cape Pacific appealed to the Appellate Division against the judgement of the trial court. The Appellate Division reversed this decision and held that the corporate veil in regard to GLI and LCI should be lifted, and ordered GLI to deliver the Findon shares to Cape Pacific. Smalberger JA delivering the majority judgement said.<sup>246</sup>

*[I]n determining whether or not having regard to the facts of each case, it is legally appropriate to disregard corporate personality one must note that the law regards the substance rather than the form of things. However the court does not have a general discretion simply to disregard a company's separate legal personality whenever it regards it as just and equitable to do so. It is nevertheless accepted that fraud, dishonesty or improper conduct could provide grounds for piercing the corporate veil. Thus, if there has been misuse of corporate personality, the court would disregard it and attribute liability where it should rightly lie. Each case would obviously have to be considered at its own merits"*

The majority judgement of the Appellate Division accepted that the law is far from settled with regard to the circumstances in which it would be permissible to pierce the corporate veil.<sup>247</sup> Thus, each case involves a process of inquiring into the facts which, once determined, may be of decisive importance. On this basis, the court laid the following principles:

- A court has no general discretion simply to disregard a company's legal personality whenever it considers it just to do so.<sup>248</sup>

---

<sup>246</sup> At 803 - 4

<sup>247</sup> At 803

<sup>248</sup> At 803

- A court should not lightly disregard a company's separate personality but should strive to give effect to uphold it.<sup>249</sup>
- Where fraud, dishonesty or other improper conduct (and the court expressly confined itself to such situations)<sup>250</sup> is found to be present, the need to preserve the company's separate personality would have to be balanced against policy considerations in favour of piercing the corporate veil.<sup>251</sup>
- A court would then be entitled to look to substance rather than form and see whether there has been a misuse of corporate personality, to disregard [the company's separate corporate personality] and attribute liability where it should rightly lie.
- Each case would have to be considered on its merits.<sup>252</sup>
- It is not necessary that a company should have been conceived and founded in deceit and never have been intended to function genuinely as a company before its corporate personality can be disregarded.<sup>253</sup>
- If a company which was legitimately established and operated is misused in a particular instance to perpetrate fraud, or dishonesty or improper purpose, its separate legal personality can be

---

<sup>249</sup> At 803

<sup>250</sup> See Williams *op cit.* 105

<sup>251</sup> See also Domanski who has argued for an approach in terms of which the policies behind recognition of a separate corporate existence must be balanced against the policies justifying piercing. He argues further that the separate entity remained a cornerstone of our company law and that the test should be applied consciously and with the protection of the separate personality as a foremost consideration at 233-235. See also *Glazer v Commission on Ethics for Public Employees* *supra*

<sup>252</sup> At 803H-804A

<sup>253</sup> See *Gilford Motor Co Ltd v Home* *supra*

disregarded in relation to the transaction in question in order to fix the individual (s) responsible with personal liability, while giving full effect to the company's separate personality in other respects.<sup>254</sup>

Williams<sup>255</sup> remarks that in applying these principles to the facts of the case, the court held that the following considerations required that the court should disregard the separate corporate identities of LCI and GLI in relation to their dealings with Findon shares:-

- The transfer of Findon shares from LCI to CLI was in fraud of the Cape Pacific's rights, at the very least it was carried out with an improper purpose, the evasion of legal obligations.<sup>256</sup> The misuse by Lubner of these two companies amounted to an abuse of their separate corporate identities. In relation to the Findon shares these two companies 'were Lubner's alter egos.'<sup>257</sup>
- Policy considerations strongly suggest that the veil of corporate personality should be pierced in relation to LCI's and GLI's fraudulent or improper dealings with the Findon shares in order to reveal Lubner as the true villain of the piece,<sup>258</sup> and
- It was within Lubner's power to compel GLI to transfer the shares to Cape Pacific.

---

<sup>254</sup> At 804B-D

<sup>255</sup> Concise Corporate and Partnership Law at 106

<sup>256</sup> See Gilford Motors's case and Jones' case, on the issue of evasion of legal obligations.

<sup>257</sup> At 804G-H

<sup>258</sup> At 804I: the court was of the view that it should not permit the notion of legal entity to be used to justify wrong, protect fraud or defend crime.

The Appellate Division strongly rejected the 'unconscionable injustice' test propounded in **Botha v Van Niekerk**.<sup>259</sup> The court found that the test was in the present case, too rigid and more flexible test should be adopted.<sup>260</sup>

The court also laid down an important principle that the piercing of the corporate veil is not precluded simply because the aggrieved party has another remedy.<sup>261</sup> As a general rule, if a person has more than one legal remedy at his disposal, he can select any of them and is not obliged to pursue one rather than another.<sup>262</sup>

Thus, if the facts of the case justify a piercing of the corporate veil, the existence of another remedy is not an absolute bar to the making of such an order. Instead it may be a relevant factor when the court considers the policy considerations of piercing the veil, but it can not be of overriding importance.<sup>263</sup>

Based on the judgement of the Appellate Division, it is the writer's submission that the trial court in refusing to lift the corporate veil, seemed to have failed to take into consideration the following factors:

- Lubner's control over the affairs of the first and second Defendants;
- The Defendant Company was the vehicle through which Lubner held his interest in the shares of the Findon Company;

---

<sup>259</sup> Supra

<sup>260</sup> At 805F

<sup>261</sup> Williams op cit.106

<sup>262</sup> At 805

<sup>263</sup> Williams op cit. 107

- The transfer of the shares in the Defendant Company was an attempt to evade the plaintiff's claim.<sup>264</sup>
- The purpose of the transfer of the shares was clearly improper.

Taking these factors into consideration, it is submitted that the trial court should have lifted the corporate veil of the first and second defendants by adopting the balancing approach (the balancing test). It is evident in this case that the strict application of the separate entity principle by the trial court led to unfair results.

The Appellate Division correctly held that the third defendant (Lubner) completely controlled the affairs of the first and second defendants. There are clear indications in this regard that Lubner was the controlling director and shareholder of the two companies.<sup>265</sup>

Perhaps the trial court should have also considered the fact that there were non-compliance with corporate formalities in respect of sale of the shares by the first defendant to the second defendant, as no board meeting was held for a resolution to be passed.<sup>266</sup>

Another factor that the trial court should have looked at is closely related to the control aspect, that is the direct intervention of the controlling shareholder (Lubner) in the affairs or transactions of the controlled company.<sup>267</sup>

Thus, Lubner conducted the affairs of the first defendant company on a personal level and the transfer of the shares from the first defendant company to the second

---

<sup>264</sup> See *Gilford Motors Ltd v Horne supra*

<sup>266</sup> See 796 D-E

<sup>267</sup> See (1996) TSAR at 159

defendant company was clearly motivated by personal reasons amounting to improper conduct.

For example, the oral instructions that were given by the Lubner to the first Defendant Company to transfer the shares to the second Defendant Company clearly constituted a direct intervention in the affairs of the Defendant Companies. On this basis, it is the writer's submission that the trial court should have lifted the corporate veil.

Thus, taking into account Lubner's control and interference in the affairs of the first and second defendants and the purpose for which this control was exercised, it is difficult to see how the first and second defendant were not used as instruments of improper conduct as the trial court decided.

It is unfortunate that the trial court had held that the first and second defendants were not the "sham", "mask" or the "alter ego" of Lubner. The court based its decision on one consideration only, being that the value of the assets of the defendants were in excess of R100 000.<sup>268</sup>

Applying the "unconscionable injustice" test<sup>269</sup> it was said that the plaintiff could not succeed because the improper conduct had not resulted in an unconscionable injustice.<sup>270</sup> The reason advanced by the trial court for this was the failure on the part of the plaintiff to act timeously to recover the shares.<sup>271</sup>

It is submitted however, that the court's argument that the conduct of the first defendant was improper and the refusal to find that the same improper conduct had

---

<sup>268</sup> At 821H-I

<sup>269</sup> See *Botha v Van Niekerk* (supra)

<sup>270</sup> At 822

<sup>271</sup> At 822

resulted in an "unconscionable injustice", begs the question, how improper must the conduct of a defendant be, before it will result in an "unconscionable injustice"?

This problem could be attributed to the trial court's failure to give a comprehensive analysis of the circumstances under which the court will regard a particular conduct as improper. The trial court failed to give an account of improper conduct, which would give rise to unconscionable injustice.

Judging from the facts of the case, it is clear that Lubner used the two companies to evade its obligations in terms of the contract. They were used merely as puppets of Lubner.<sup>272</sup> Thus, his direct intervention in the affairs of the first and second defendants proved to be evidence of his control. Therefore, a refusal to lift the veil under these circumstances left the plaintiff without a proper remedy.

Had all these factors considered in the totality, bearing in mind the purpose of the lifting (the balancing test), the trial court should have found that the strict application of the separate entity principle led to inequitable result. Although the trial court considered a variety of factors, however in the final analysis, it based its refusal to lift the corporate veil on a single factor.<sup>273</sup>

The Appellate Division regarded an approach which involves a balancing of policy considerations in favour of and against piercing the corporate as being the appropriate in determining whether the separate legal existence of a company should be disregarded in cases involving fraud, dishonesty or other improper conduct.<sup>274</sup> Based

---

<sup>272</sup> (1996) TSAR at 160

<sup>273</sup> This clearly not in accordance with the balancing test propounded by the Appellate Division.

<sup>274</sup> At 803 H-J

on this, it is the writer's submission that the approach followed by the Appellate Division is correct.

Having considered the majority judgement, there is much to be said for the rather conservative approach to piercing the corporate veil, sets out in the minority judgement of Van Heerden JA.<sup>275</sup>

The judge concluded that fraud was not the only instance in which the corporate veil could be lifted. He said that the corporate veil could be lifted, where special circumstances existed, which would indicate that the company is a mere façade, concealing the true state of affairs. Thus, it is only appropriate to pierce the corporate veil where special circumstances exist.<sup>276</sup>

However, Van Heerden JA said that based on the facts, there was no evidence of "façade".<sup>277</sup> Thus, neither the transfer of Findon shares nor the fact that Lubner controlled LCI and GLI was a secrete. He concluded that the mere fact that Lubner was in control and that the transfer of shares was effected with the intention of thwarting Cape Pacific's rights, did not justify the lifting of the veil.<sup>278</sup>

The writer respectfully submits that the approach adopted by the minority judgement is too narrow. Thus, taking into account Lubner's control and interference in the affairs of LCI and LGI, it is difficult to conceive how the two companies were not used as devices or instruments in the furtherance of the business and interest of Lubner. There is

---

<sup>275</sup> At 811

<sup>276</sup> At 811

<sup>277</sup> At 811-13

<sup>278</sup> At 813

evidence, which suggests that Lubner did not treat the two companies as separate entities. In the circumstances, the minority judgement should not be followed.

#### 7.4 Summary

Williams argues that the major significance of the decision in Cape Pacific is that it affirmed that although a company is a legal persona in its own right, courts have the power at common law, to pierce the corporate veil, but will not lightly do so.<sup>279</sup> For example, the court may exercise its discretion to pierce the corporate veil where there has been fraud, dishonesty or other improper conduct. But, the Appellate Division made it clear that these were not necessarily the only categories of conduct, which warranted a piercing of the veil.<sup>280</sup>

It is further submitted that the judgement represents a move away from the categorising approach toward a balancing of the need to preserve the separate

---

<sup>279</sup> Concise Corporate and Partnership Law at 107. Although the court did not see appropriate to lay down an exhaustive and definite catalogue of the circumstances in which the court will lift or pierce the corporate veil, it appears that conduct which falls short of fraud will suffice, bearing in mind that the minority judgment in Cape Pacific case alluded to the fact that such conduct should not be confined only to fraud.

<sup>280</sup> Williams op cit. at 107. The court stated that each case would have to be decided according to its own facts. At least in the circumstances of the Cape Pacific case the Appellate Division did not see appropriate to apply the 'unconscionable injustice enunciated in *Botha v Van Niekerk supra*. The court expressed the view that this test was too narrow and a more flexible approach was needed.

corporate identity against the policy considerations in favour of piercing the veil in a particular case.<sup>281</sup>

After the decision in *Cape Pacific* there is in our law a doctrine of piercing the corporate veil, which truly requires the court to take into consideration competing issues before it could disregard the separate existence of a company as a legal persona.

For example, in **Le Bergo Fashions CC v Lee & Another**<sup>282</sup>, the court refused to allow a shareholder to use her company as a "facade" in an attempt to breach a contract, which she had concluded with the plaintiff. The shareholder had entered into a restraint of trade agreement in her own name, and had then attempted to use her company to evade her obligations in terms of the agreement.

The court, following the decision in the *Cape Pacific* case, justified a piercing of the corporate veil on the basis of improper conduct, which it said was not the same as fraud or dishonesty.<sup>283</sup> The court held that even though the company had not been a party to the restraint agreement, nevertheless its conduct was such that it amounted to intentionally assisting the shareholder to evade her legal obligation in terms of the agreement.<sup>284</sup>

It seems that the balancing approach adopted in *Cape Pacific* case at least introduces flexibility and some interesting developments in the piercing law and probably attempts

---

<sup>281</sup> Williams *op cit.* at 107. Domanski has argued for an approach in terms of which the policies behind recognition of a separate corporate existence must be balanced against the policies justifying piercing.

<sup>282</sup> 1998 (2) SA 608 (C)

<sup>283</sup> At 613H

<sup>284</sup> See *Gilford Motors Ltd*, *supra*

to bring certainty and clarity into the law.<sup>285</sup> One might see in the approach of the Appellate Division in *Cape Pacific* a pattern for a very fruitful approach to all difficult questions, which are posed by the veil piercing doctrine.

However, whether there is wisdom in this development is a different question. The justification for piercing the veil of corporate personality in relation to common law has never been an easy issue for courts to deal with. Even the Appellate Division in *Cape Pacific* case accepted that the law is far from settled with regard to the circumstances in which it would be permissible to pierce the corporate veil.<sup>286</sup> The Appellate Division was not prepared to commit itself or to lay down or even to identify a general principle for piercing or lifting the corporate veil.<sup>287</sup>

---

<sup>285</sup> Domaski op cit. at 235.

<sup>286</sup> At 803

<sup>287</sup> At 803B-C

## CHAPTER 8

### 8.1 GENERAL SUMMARY

The discussion above has canvassed that common law empowers a company to be viewed in its separate state. The judgement of *Salomon v A Salomon Co Ltd*<sup>288</sup> is primarily associated with the salutary company-law that a company even closely controlled, is a legal entity distinct from its members.

It follows that the members of a company are not liable per se for the debts of the company. In fact the major reason for forming a company in many instances is that members wish to limit their liability, should the company incur losses.

It has been also canvassed that a corporate veil falls between the corporation as a separate entity and its members in such a way that it hides members from the view of outsiders looking at the corporation.

But, at the same token, members of a company are prevented from using the property of the company as they wish. The property of a company belongs to it and not to its members. It follows that the profit made by the company belongs to it.

Thus, no members can regard the company's assets or profit as his own regardless of the extent of his interest in or control over the affairs of the corporation. Any member or director who fails to adhere to this principle may be held personally liable for what appear to be acts or obligations of the company.

The discussion above has canvassed that the justification for piercing or lifting the corporate veil in terms of common law has never been an easy issue for courts to deal

---

<sup>288</sup> Supra

with. This problem can be observed not only in South Africa but also in other jurisdictions, especially in England.

In the context of England, the problem could be attributed to the fact that courts have relied invariably on a number of separate and unrelated categories of conduct upon which to base decisions to pierce the corporate veil.

It has been argued that the categorising approach is unsatisfactory, simply because most of the categories sometimes overlap and many do not articulate the principle upon which they are decided. The major problem with the categorising approach is that it may lead to a strict approach.

The same is true in the context of South Africa. It has been canvassed that similar to their English counterparts, courts in South Africa have chosen to rely on a number of discrete, unrelated categories of conduct as grounds for piercing the corporate veil. But, it has been shown that fraud, improper conduct and the abuse of corporate personality are the most commonly used forms of categories.

For example, the decision in *Lategan* vividly exemplifies the tendency of the courts in South Africa to rely on the categorising approach (fraud). It also vividly highlights the problem associated with the categorising approach, that it may lead to a narrow approach, especially in those instances, where there has been no fraud perpetrated by the members of the corporate entity.

The same is true in regard to the "unconscionable injustice" propounded in *Botha's* case.<sup>289</sup> It has been argued that the test of unconscionable injustice affords little assistance in defining the circumstances in which it would be justifiable to pierce or lift the corporate veil. In essence, it does not give pause to our criticisms of piercing the

---

<sup>289</sup> *Supra*

corporate veil. Implicit in this test is the creation of a new piercing category, which is admittedly wider than mere fraud, but a category nevertheless.<sup>290</sup>

In a nutshell, the test formulated in Botha fails to define what acts constitute improper conduct or what conducts would trigger the piercing of the corporate veil nor does the test define what unconscionable injustice mean.

Overall the test formulated in Botha is not bidding, as the court did not see the facts as calling for piercing the corporate veil. This became evident when the Appellate Division in Cape Pacific case rejected the test. The Appellate Division confirmed that the unconscionable test was too rigid to be applied in the case before it.

It has been argued further that the lack of a single principle has brought an element of inconsistency and uncertainty into the piercing law of both England and South Africa. It has been canvassed that courts can learn from the American jurisprudence. As far back as 1983, The American courts boldly introduced a more detailed approach (the balancing test),<sup>291</sup> which at least attempts to weigh up factors that are relevant to the enquiry (piercing the corporate veil).<sup>292</sup>

It seems that the balancing approach introduces flexibility into the law, and probably articulates what courts ought to do in piercing cases. In terms of this approach, the policies behind recognition of a separate corporate existence must be balanced against the policies justifying piercing the corporate veil.

It has been argued that the balancing test requires an evaluation of competing policy considerations in order to determine whether or not the veil of incorporation should be

---

<sup>290</sup> See Domaski op cit. at 228.

<sup>291</sup> See *Glazer v Commission on Ethics for Public Employees*, supra

<sup>292</sup> See Milo op cit. at 76

disregarded. It has been also argued that at least the balancing approach compels the ventilation of the contested issues.

It has been canvassed in this research that there have been some interesting developments in the piercing law of South Africa. It seems that our courts have learnt from the American jurisprudence. The leading piercing case in South Africa is the *Cape Pacific*,<sup>293</sup> where the Appellate Division clearly adopted and followed the balancing approach.

Thus, the court in the *Cape Pacific* proposed to do no more than applying what it conceived to be the appropriate legal principle to the facts of the case (the balancing test).

It has also been argued above that the decision in the *Cape Pacific* affirms that although a company has a legal personality on its own right, courts have the power at common law to pierce the corporate veil, but will not lightly do so. Fraud, dishonesty or other improper conducts are not necessarily the only grounds, which trigger a piercing of the veil.

---

<sup>293</sup> *Supra*

## 8.2 Conclusion

The balancing approach should be followed in South Africa. This approach is qualitatively different from the traditional categorising approach because it attempts to unify and rationalise decisions on the basis of a single underlying principle. It may prove capable of bringing order, certainty and consistency into this area of law, the judicial disregarding of the separate legal personality.

However, the fact that the Appellate Division expressed a view that the law is far from settled with regard to the circumstances in which it would be permissible to pierce the corporate veil, begs the question whether there is wisdom in the development discussed above.

Given the fact that in the decision of the Cape Pacific, the Appellate Division was not prepared to commit itself to lay down or even to identify a general principle regarding the lifting of the corporate veil, indicates that there is need to ask this question.

Perhaps the justification given by the Appellate Division for not identifying the general principle that there is no use to try to fit the facts of a particular case into an existing category of circumstances or to introduce a new category, gives an answer to the question posed.

Nevertheless, we still lack a single coherent principle upon which to base decisions to pierce the corporate veil in terms of common. One hopes that the balancing approach will be allowed to live on in the future.

**BLIBLIOGRAPHY**

1. Beale, JH *A Selection of Cases on the Conflict of Laws* 2ed (1907), Harvard University Press
2. Beuthin, RC *Basic Law* 2ed (1997) Butterworths, Durban
3. Bolter, JJ *Piercing the Corporate Veil* (1994) Annual Survey of South Africa 409-16
4. Chardwick, NL. *Lifting the Corporate Veil* (1974) 14 Rhodesian Law Journal 37-43
5. Cilleirs, JB & Luitz, SM *The Corporate Veil, Unnecessary Confining Corset?* (1996) 56 THRHR 523-29
6. Cilliers, HS & Benade, ML *Company Law* 3ed. (1977) Butterworths, Durban
7. Cilliers, HS & Benade, ML *Company Law* 4ed (1982) Butterworths, Durban
8. Cilliers, HS & Benade, ML *Company Law* 5ed (1984) Butterworths, Durban
9. Cillies, P *The New Company Law* (1989) Butterworths, Durban
10. Clark, RC *Corporate Law* (1986) Little Brown & Company
11. Davids, C *The Lingering question: Some Perspective on the Lifting of the Corporate Veil* (1994) TSAR 36-40
12. Domanski, A *Piercing the Corporate Veil-A new direction* (1986) 103 South African Law Journal 224-227
13. Farrar, JH *Farrar's Company Law* 3ed. (1991) Butterworths, London
14. Ford, HA *Principles of Company Law* 2ed. (1978) Butterworths, Sydney

15. French, HL *Case Book on Australian Corporation Law* 5ed. (1991) Butterworths, Sydney.
16. Gallagher, L & Ziegler, P *Lifting the Corporate Veil in the Passion of Justice* (1989) *Journal of Business Law* .
17. Gibson, J *South African Mercantile & Company Law* (1997) Juta & Company, Johannesburg.
18. Gower, LCB *Gower's Principles of Modern Company Law* 4ed (1979) Stevens & Sons, London (Cited as Gower Modern Company Law)
19. Gullick, JM *Ranking & Spiers' Company Law* 2ed. (1997) HFL Publishers Limited.
20. Joubert, WA *The Law of South Africa (Law of South Africa (LAWSA) vol.4 Part 1*(1995)
21. Hahlo, HR *Hahlo's South African Law Through the cases* 5ed (1991) Juta & Company.
22. Larkin, *Regarding Judicial Disregarding of the Company's Separate Identity, Piercing the Corporate Veil* (1989) *SA Mercantile Law Journal* 227 -238
23. McLennan, J *The Liability of Agents for Debts Contracted on Behalf of Insolvent Companies* (1998) *South African Law Journal (SALJ)* 68-73
24. Milo, D *The liability of a Holding Company for the Debts of its Subsidiary: "Is Salomon still alive and well"?* (1998) *South African Law Journal (SALJ)* 326-346
25. Morse, G *Charleworth & Morse Company Law* 14 ed. (1991) Stevens & Sons, London

26. Ottelenghi, S *'From Peeping behind the Corporate Veil to ignoring it Completely'*  
3ed. (1990) *Modern Law Review* 338-44
27. Pennington, H *Principles of Company Law* 5ed. (1985) Butterworths, London
28. Powles, D *The see-through Corporate Veil* (1977) 40 *Modern Law Review* 339-46
29. Pyne, J *Lifting the Corporate Veil: A Reassessment of the Fraud Exception* (1997)  
56 *Cambridge Law Journal* 228-36
30. Sealy, LSS *Corporate Personality in the 20<sup>th</sup> Century* (1997) 58 *Cambridge Law  
Journal* 247-53
31. Sher, H *Piercing the Corporate Veil* (1994) *Business Law Journal* 51-60
32. Schoeman, *Guide to the Close Corporations Act and Regulations*, Service No: 11  
(2000)
33. Williams, RC *Concise Corporate & Partnership Law* 2ed (1997) Butterworths,  
Durban
34. Van Wyk, S *Corporate Personality and a Comparative Overview of the Judicial  
Disregarding of the Corporate Veil* (1992) University of Natal Law Library
- 3.3 Wolff, M *On the Nature of Legal Persons* (1938) *Law Quarterly Review* 494-505

**TABLE OF CASES****A**

*Adams v Cape Industries* [1990] Ch 433

*Atlas Maritime Co SA. v Avalon Maritime Ltd (No.1)* [1991] 4 ALL ER 769

**B**

*Botha v Van Niekerk en ander* 1983 (3) SA 513 (W)

*Briggs v James Hardie & Co (Pty) Ltd* [1989] 16 NSWLR 549

*Belars v Hodnett* 1978 (1) SA 1109 (A)

**C**

*Cape Pacific v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A)

*Caxton Limited v Reeva Forman (Pty) Limited* 1990 (3) 547 (A)

*Cattle Breeders Farm (Pty) Ltd v Veldman* 1974 (1) SA 169 (RA)

**D**

*Dadoo (Pty) Limited v Krugersdorp Municipal Council* 1920 AD 530

*Daimler Co Ltd v Continental Tyre & Rubber Co Ltd* [1916] 2AC 307

*DHN Food Distributors Ltd v London Borough of Tower Hamlets* [1976] 3 ALL ER 462  
(CA)

*Dhlomo No V Natal Newspapers (Pty) Ltd* 1989 (1) SA 547 (A)

## F

*Fairlane Shipping v Adamson* [1974] 2 ALL ER 767 (QB)

*Financial Mail (Pty) Ltd v Sage Holdings Ltd* 1993 (2) SA 452 (A)

*Food & Nutritional Products Limited v Neuman* 1986 (3) SA 464 (W)

*Foss v Harbottle* [1845] 2 Hare 461, 67 ER 189

*Fowler v Commercial Timber* [1930] 2KB 1

## G

*Gilford Motor Co v Home* [1933] Ch 945 (CA)

*Glazer v Commission on Ethics for Public Employees* [1983] 431 SO 29

*Gumede v Bandhla Vukani Bakithi Limited* 1950 (4) SA 560 (N)

*Genwest Batteries (Pty) Ltd v Van der Heerden* 1991 (1) SA 727 (T)

## H

*Hilton v Plustile* [1989] 1 WLR 149

## I

*In re Yenidje Tobacco Ltd* [1916] 2Ch 426 (CA)

## J

*Jones v Lipman* [1962] WLR 832

## L

*Lawrence v Lawrich Motors (Pty) Ltd* 1948 (2) SA 1029

*Le Bergo Fashions CC V Lee* 1998 (2) SA 608 (C)

*Lee v Lee's Air Farming Limited* [1961] AC 12 (PC)

*Letegan v Boyes* 1980 (4) SA 191 (T)

## M

*Maasdorp v Harddow NO* 1959 (3) SA 861 (C)

*Madra Anjuman Limited v Johannesburg Municipal Council* 1919 AD 439

*Macaura v Northern Assurance Company Ltd* [1925] AC 619

*Motors Industry Fund Administrators (Pty) Ltd v Janit* 1994 (3) SA 56 (W)

*Moosa v Mavjee Bhawan (Pty) Ltd* 1966 (4) SA 462 (T)

*Muller v Coca-Cola SABCA (SA) (Pty) Ltd* 1998 (2) SA 824 (SE)

## O

*Orkin Bros Limited v Bell* 1912 AD 198

## P

*Pressma Services (Pty) Ltd v Schutter* 1990 (2) SA 411 (C)

## R

*Re Bugle Press Ltd* [1961] Ch 270 (CA)

*Re A Company* [1985] BCLC 333 (CA)

*Re Darby Ex Parte Brougham* [1911] 1 KB 95

*Ritz Hotel v Charles of the Ritz Ltd* 1988 (3) SA 290 (A)

*Robinson v Randfontein Estate Gold Mining Co Ltd* 1921 AD 168

*R v Gillette* 1929 AD 364

S

*Salomon v A Salomon & Co Ltd* [1897] AC 22 (HL)

*Shipping Corporation of India Ltd v Eudomen Corp* 1994 (1) SA 550

*Smith, Stone & Knight Ltd V Birmingham Corporation* [1939] 4 ALL ER 116

U

*Universiteit van Pretoria v Tommie Meyer Films* 1979 (1) SA 44 (A)

V

*Von Wulfflig-Eybers v Sound-Props 2587 Investments CC* 1994 (4) SA 640 (C)

W

*Wallersteiner v Moir* [1974] 3 ALL ER 217 (CA)

•

## **TABLE OF STATUTES**

Companies Act 61 of 1973

Close Corporations Act 69 of 1984