THE SUPREME COURT OF APPEAL
REPUBLIC OF SOUTH AFRICA

JUDGMENT

Case number: 485/2007

In the matter between:

NIZAAR EBRAHIM First appellant

ABBAS EBRAHIM Second appellant

and

AIRPORTS COLD STORAGE (PTY) LTD Respondent

Neutral citation: *Ebrahim v Airports Cold Storage (Pty) Ltd* (485/2007) [2008] ZASCA 113 (25 September 2008)

BEFORE : **Harms ADP, Cameron JA, Ponnan JA, Mlambo JA and Mhlantla AJA**
HEARD : **Tuesday 26 August 2008**
DELIVERED : **Thursday 25 September 2008**

SUMMARY: Corporation – Close Corporations Act 69 of 1984, s 64(1) – reckless carrying on of business – liability for debts – member of corporation and father – corporation run without books or documentation – debt of another corporation transferred to it without consideration – reckless trading established

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ORDER

On appeal from the High Court, Cape Town (Griesel J sitting as a judge of first instance):

The appeal is dismissed with costs.

JUDGMENT

CAMERON JA (Harms ADP, Ponnan JA, Mlambo JA and Mhlantla AJA concurring):

[1] The appellants, Mr Nizaar Ebrahim and Mr Abbas Ebrahim, son and father, appeal with leave granted by Griesel J against a judgment in the High Court in Cape Town in which he declared them personally liable for a debt a close corporation incurred during its short operational life in 2005.[1] For three months from March of that year the respondent (plaintiff) supplied Sunset Beach Trading 232 CC (trading as 'Global Foods') (the CC) with frozen meat, poultry and other comestibles. Payments initially flowed, but slowed to a trickle and eventually dried up in June, when invoices totalling R278

[1] *Airport Cold Storage (Pty) Ltd v Ebrahim and others* 2008 (2) SA 303 (C).

377,19 were still outstanding. In response, the plaintiff moved to liquidate the CC. It obtained a final winding-up order in September. But the cupboard was bare: despite recorded deliveries invoiced at over R1,8 million, the cash in hand totalled only R254,99. The CC had no other assets.

[2] The plaintiff then brought this action to recover the debt from Nizaar (Ebrahim junior), who was the CC's sole member, and his father Abbas (Ebrahim senior). (The CC's liquidator was joined formally as third defendant, but takes no part in the appeal.) The plaintiff targeted Ebrahim senior on two and Ebrahim junior on three alternative bases:

(a) That both were personally liable under s 64(1) of the Close Corporations Act 69 of 1984 (the Act) because during the period March to August 2005 the CC's business was conducted recklessly or for fraudulent purposes or with intent to defraud its creditors. Section 64 of the Act reads:

> (1) If it at any time appears that any business of a corporation was or is being carried on recklessly, with gross negligence or with intent to defraud any person or for any fraudulent purpose, a Court may on the application of the Master, or any creditor, member or liquidator of the corporation, declare that any person who was knowingly a party to the carrying on of the business in any such manner, shall be personally liable for all or any of such debts or other liabilities of the corporation as the Court may direct, and the Court may give such further orders as it considers proper for the purpose of giving effect to the declaration and enforcing that liability.
> (2) Without prejudice to any other criminal liability incurred where any business of a corporation is carried on in any manner contemplated in subsection (1), every person who is knowingly a party to the carrying on of the business in any such manner, shall be guilty of an offence.

(b) That both were personally liable under s 65 because their incorporation and use of the CC constituted a gross abuse of the juristic personality of the CC as a separate entity.[2]

(c) That as a member Ebrahim junior was in addition liable under s 63(h) of the Act because he allowed the office of accounting officer of the CC to remain vacant for more than six months.[3]

[3] At the trial, the plaintiff's managing director, Mr Patrick Gaertner, testified, as well as an accountant, Mr Derek John Hanslo, who gave expert testimony on business practice and bookkeeping requirements, and an employee from the firm of liquidators managing the liquidation, Mr JJ Theron. For the defendants the only witness was Mr Nasief Price, an accountant. Neither of the Ebrahims gave evidence. Plaintiff's

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[2] Close Corporations Act 69 of 1984 s 65:
'**Powers of Court in case of abuse of separate juristic personality of corporation**
Whenever a Court on application by an interested person, or in any proceedings in which a corporation is involved, finds that the incorporation of, or any act by or on behalf of, or any use of, that corporation, constitutes a gross abuse of the juristic personality of the corporation as a separate entity, the Court may declare that the corporation is to be deemed not to be a juristic person in respect of such rights, obligations or liabilities of the corporation, or of such member or members thereof, or of such other person or persons, as are specified in the declaration, and the Court may give such further order or orders as it may deem fit in order to give effect to such declaration.'

[3] Close Corporations Act 69 of 1984 s 63:
'**Joint liability for debts of corporation**
Notwithstanding anything to the contrary contained in any provision of this Act, the following persons shall in the following circumstances together with a corporation be jointly and severally liable for the specified debts of the corporation: …
(h) where the office of accounting officer of the corporation is vacant for a period of six months, any person who at any time during that period was a member and aware of the vacancy, and who at the expiration of that period is still a member, shall be so liable for every debt of the corporation incurred during such existence of the vacancy and for every such debt thereafter incurred while the vacancy continues and he or she still is a member.'

counsel had however examined them under sub-poena at the statutory inquiry[4] held in the wake of the CC's liquidation, and the transcript was admitted at the trial.[5]

[4] Griesel J found that despite denials by both Ebrahims, it was clear that Ebrahim senior had actively assisted his son in running the CC, as well as in various other family businesses. Going back to 1997, he found, the father and the rest of the family had used 'a host of entities and trading names at different stages' to pursue their business interests, and that in doing so they had 'scant regard' for the entities' separate corporate identities. Griesel J upheld the action on all three bases of complaint. He found that the causes of action formed part 'of one composite complaint of abuse of the separate juristic personality' of the CC. The CC had no accounting officer; it was started for a fraudulent reason; and the Ebrahims had traded recklessly through it, in insolvent circumstances, without the requisite belief that it would be able to pay its debts as they fell due. Although they attempted to obtain the advantages of separate identity, he found that they operated its

[4] Companies Act 61 of 1973 s 415 '**Examination of directors and others at meetings**' [which in terms of s 66 of the Close Corporations Act 69 of 1984 applies mutatis mutandis] provides that any creditor who has proved a claim against a close corporation may at a creditors' meeting interrogate any person sub-poenaed 'concerning all matters relating to the company or its business or affairs'.

[5] Section 68(1) of the Insolvency Act 24 of 1936, read with s 339 of the Companies Act 61 of 1973 and s 66 of the Close Corporations Act.

business as if it were their own and without due regard for or compliance with statutory and bookkeeping requirements. He dismissed the Ebrahims' belated challenge to the quantification of the debt the CC owed, and gave judgment against them for the full amount claimed.

[5] On appeal, the Ebrahims put in issue these findings, disputing that there was abuse of corporate form or that, if there was, it had any causal impact on the plaintiff's claim. They contend moreover that the plaintiff was aware of the CC's 'normal' trading practices – yet continued to trade with it until the plaintiff was itself unable to supply further stock to the CC: this they say precipitated the CC's cash flow crisis, which in turn led to its inability to repay the plaintiff.

[6] To take the proper measure of the defendants' argument, it is necessary to sketch the background to the parties' dealings. Gaertner testified that he had done business with the Ebrahims since about 1997 (Ebrahim senior dated their connection back to considerably earlier). Though he dealt with the defendants through various entities, the business was the same: the sale of bulk imported frozen comestibles and other goods. The transactions were always concluded with Ebrahim senior – each Monday he would meet with him to finalise orders. It was

he who had to confirm the price, and who would thereafter return the signed confirmation of sale to the plaintiff.

[7] During late 2004, Gaertner explained, the plaintiff required a VAT number for the entity the plaintiff was then supplying, Zaki Meat Market CC (Zaki). The number Ebrahim senior gave to Gaertner was invalid, but he volunteered that a different entity, the CC, had a valid number. Hence, Gaertner testified, the plaintiff agreed to start channelling the Ebrahims' orders through the CC from March 2005.

[8] A considerable volume of business was transacted through the CC from late March until, after payments faltered, the last sale took place on 24 June 2005. However, the evidence the plaintiff presented revealed that the CC's affairs were anything but tightly run.

[9] Hanslo testified that the sole business records of the CC consisted in Croxley invoice books. Although the CC had charged its customers value-added tax (VAT), no VAT returns were submitted to the South African Revenue Services (SARS), and no VAT payments were made. Hanslo calculated that some R200 543,59 was due to SARS. The CC's defence, ineffectually advanced during Hanslo's cross-examination and in the evidence of Price, was that since VAT returns were

required to be submitted only every two months, and VAT paid only once a year, the short operational life of the CC rendered the omissions insignificant. This ignores the fact that not only did the CC fail to submit VAT returns, but it failed to record anywhere that it was collecting VAT from its customers. The suggestive (if not compelling) inference is that there was never any intention to pay VAT.

[10] The CC's business appears to have been conducted with blithe disregard of statutory requirements. There were no conventional books of account. Apart from its payments to the plaintiff and to a cold storage facility, there was not a single record of any expense recorded in any documents provided after liquidation. Even though the employee complement numbered between ten and twenty, there were neither payslips nor pay-as-you-earn (PAYE) returns. In violation of s 56 of the Act, no proper 'accounting records' were kept; nor was there an accounting officer.

[11] Payments to creditors totalled just over R1,4 million, against income in excess of R1,8 million. The latter figure – reflecting Hanslo's detailed examination of invoices against which payment had been received – gave rise to two signal conclusions set out in Hanslo's evidence:

(a) The first was that only a small portion (less than 10%) of the CC's cash takings and other receipts was deposited into any bank account. (The portion that was, found its way into another of the Ebrahims' CCs.) The reason the Ebrahims advanced – avoidance of bank charges and cash deposit fees – Hanslo treated with reserve, since, he pointed out, the sheer volume of money received over the period in question rendered the bank-free approach 'most unusual'.

(b) The second conclusion to which Hanslo deposed was that the CC's vouched receipts and expenditures indicated that when trading ended there should have been a positive balance of some R300 000 'in a bank account or on hand'. Instead, there was only R254,99. This meant that some R300 000 was missing. Hanslo dryly suggested that 'it's sitting in a drawer somewhere'. Of course no one could establish which drawer. Taxed with this during his examination at the inquiry, Ebrahim junior ingenuously protested, 'I mean, I don't understand, are you trying to accuse me of hiding cash?' That was indeed the accusation, and in the absence of any other explanation it sticks.

[12] To Hanslo's exposition Theron added that while the fact that the CC had no financial statements was explicable in view of its

short operational span, the sole record of trading activity was the invoice books: there were no other management records or reports of daily sales, itemised expenses, a trial balance or balance sheet.

[13] On this foundation, the plaintiff contended it had established that the business of the CC was 'carried on recklessly' within the meaning of s 64 of the Act, and indeed that it had made out a case of fraudulent trading. Section 64 is for all intents and purposes identical to s 424 of the Companies Act 61 of 1973,[6] 'at least as far as the underlying philosophy is concerned'.[7] The case law on one provision therefore illuminates the other.[8] The Act adds 'gross negligence' to the Companies Act's list of impugned business methods. Whether there is a meaningful difference between recklessness and gross negligence in this context need not be decided now.[9]

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[6] Companies Act 61 of 1973, s 424:
'**Liability of directors and others for fraudulent conduct of business**
(1) When it appears, whether it be in a winding-up, judicial management or otherwise, that any business of the company was or is being carried on recklessly or with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the Court may, on the application of the Master, the liquidator, the judicial manager, any creditor or member or contributory of the company, declare that any person who was knowingly a party to the carrying on of the business in the manner aforesaid, shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Court may direct.'

[7] *Saincic and Others v Industro-Clean (Pty) Ltd* (229/05) [2006] ZASCA 83; [2006] SCA 77 (RSA) (31 May 2006) para 27 per Harms JA.

[8] See the approach this Court adopted in *L&P Plant Hire BK v Bosch* 2002 (2) SA 662 (SCA) para 39.

[9] See the discussion in *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA), where Howie JA noted that 'the ordinary meaning of "recklessly" includes gross negligence' (at 143F), and that recklessness itself connotes 'at the very least gross negligence' (at 144A).

[14] Acting 'recklessly'[10] consists in 'an entire failure to give consideration to the consequences of one's actions, in other words, an attitude of reckless disregard of such consequences'.[11] In applying the recklessness test to the running of a closed corporation, the Court should have regard to amongst other things the corporation's scope of operations, the members' roles, functions and powers, the amount of the debts, the extent of the financial difficulties and the prospects of recovery, plus the particular circumstances of the claim 'and the extent to which the [member] has departed from the standards of a reasonable man in regard thereto'.[12]

[15] It need hardly be added that the function of the statutory provision also shapes its application. Although juristic persons are recognised by the Bill of Rights – they may be bound by its provisions,[13] and may even receive its benefits[14] – it is an apposite truism that close corporations and companies are imbued with identity only by virtue of statute. In this sense their separate existence remains a figment of law, liable to be

[10] *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA) 143F-G.
[11] *S v Dhlamini* 1988 (2) SA 302 (A) 308D-E, applied in the corporate context in *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA) 143F-G.
[12] *Fisheries Development Corporation of SA Ltd v Jorgensen* 1980 (4) SA 156 (W) 170B-C, per Margo J, adopted in part in *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA) 144B.
[13] Bill of Rights s 8(2): 'A provision in the Bill of Rights binds a natural or a juristic person if, and to the extent that, it is applicable, taking into account the nature of the right and the nature of any duty imposed by the right.'
[14] Bill of Rights s 8(4): 'A juristic person is entitled to the rights in the Bill of Rights to the extent required by the nature of the rights and the nature of that juristic person.'

curtailed or withdrawn when the objects of their creation are abused or thwarted. The section retracts the fundamental attribute of corporate personality,[15] namely separate legal existence, with its corollary of autonomous and independent liability for debts, when the level of mismanagement of the corporation's affairs exceeds the merely inept or incompetent and becomes heedlessly gross or dishonest. The provision in effect exacts a quid pro quo: for the benefit of immunity from liability for its debts, those running the corporation may not use its formal identity to incur obligations recklessly, grossly negligently or fraudulently. If they do, they risk being made personally liable.

[16] This is a good case in point. The CC was lifted from its shelf existence in early 2005 for the expedient but legitimate purpose of providing the Ebrahims' creditors with a valid VAT number. As Gaertner testified, it made no difference to him through which entity his enterprise was credited for the comestibles the Ebrahims ordered; he merely wished to supply a valid VAT number when claiming his own input tax credits. Thus far, the change of corporate vehicle was contrived but permissible. But

[15] Paul L Davies *Gower & Davies, Principles of Modern Company Law* 8 ed 2008 ch 2 para 2–1, p 33.

the Ebrahims then over-stepped the bounds. They transferred to the CC the entire debt owed to the plaintiff by the entity with which the plaintiff had till then been trading, Zaki. This was an amount in excess of R600 000. The CC received no consideration for taking over Zaki's debt. The Ebrahims just did it.

[17] With commendable candour, Ebrahim junior avowed that he regarded the transfer of Zaki's debt to the CC as 'just a formality'. This was plainly truthful. For him the CC was simply a shell and a shape, for ad hoc use at the convenience of the Ebrahims' trading circumstances. The transcription of the debt was merely a book entry made against one book entity rather than another. But what this showed equally plainly is that he had no conception of, nor respect for, the fact that the CC was a distinct legal entity with a separate legal existence; that to sustain its separateness the law exacts compliances and formalities; and that it could not be used at will as the receptacle of another entity's accumulated debts.

[18] The statutory provision targets just such heedlessness of corporate autonomy and form. The transfer of Zaki's debt without any quid pro quo showed reckless disregard for the CC's solvency, for its ability to repay the debts it incurred, and

for its capacity as a legal entity to accumulate and preserve assets of its own. (It is no doubt with an eye to the importance of a corporate entity's independent asset-accumulating capacity that Henochsberg says that 'recklessly' means carrying business on 'by conduct which evinces a lack of any genuine concern for its prosperity'.)[16]

[19] Having started by fecklessly encumbering the CC with a massive debt, everything else the Ebrahims did in relation to it manifested more of the same. Their stewardship failed to pay heed to the consequences of their actions for the CC's independent well-being. Its entire existence was, in Ebrahim junior's telling words, 'just a formality'. This explains the failure to keep any records or accounts or to keep track of cash and other receipts. The consistent disregard of the independent well-being of the CC as a separate entity constituted reckless carrying on of its business as contemplated by s 64. And it is clear that this manner of doing business is what left the plaintiff out of pocket.[17]

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[16] *Henochsberg on the Companies Act*, edited by JA Kunst and others, service issue 27, June 2008, p 916. The statement has been judicially approved on more than one occasion.

[17] *Saincic and Others v Industro-Clean (Pty) Ltd* (229/05) [2006] ZASCA 83; [2006] SCA 77 (RSA) (31 May 2006) para 29 per Harms JA, pointing out that 'the provision could not have intended that causation [between the impugned conduct and the unpaid debt] does not play any role at least as far as creditors are concerned'.

[20] The Ebrahims' defence on the Zaki debt transfer – that Gaertner and the plaintiff were party to the re-invoicing of the amount owing – finds no purchase. Gaertner was not running the CC. More pertinently, he was not privy to the arrangements the Ebrahims might properly have made for securing the CC's legitimate interests when the debt was transferred. His interest, as a creditor, was in getting paid. No more was expected from him. There was no suggestion that he participated in a scheme to defraud the CC or colluded in the Ebrahims' management of the enterprise. In the absence of such evidence his knowledge of the transfer cannot diminish the plaintiff's entitlement to be repaid.

[21] It is equally ineffectual in response to the invocation of s 64 to say that the plaintiff and Gaertner could have safeguarded their risk by exacting suretyships from the Ebrahims for the CC's debts. That may have saved the plaintiff a lot of trouble, as well as the expense of a protracted trial. But it is no answer to a creditor's legitimate reliance on s 64 to say that it could have chosen a shorter or wiser route. The provision's objectives, which are both compensatory[18] and punitive,[19] play

[18] MS Blackman and others *Commentary on the Companies Act* (2002, with updates) vol 3 14–524
[19] *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA) 142H-I.

an important role in reminding those who run corporations, and those knowingly party to their business methods, that the shadow of personal liability can fall across their dealings.

[22] In contrast with the United Kingdom, where it seems the equivalent provisions have in recent years 'been very rarely used' to fasten directors with personal liability,[20] the jurisprudence of this Court evidences claimants' spirited reliance on the provision. Though courts will never 'lightly disregard' a corporation's separate identity,[21] nor lightly find recklessness,[22] such conclusions when merited can only help in keeping corporate governance true. They are certainly fitting here.

[23] The finding by Griesel J that Ebrahim senior was deeply involved in the running of the CC entails ineluctably that he had knowledge of the relevant facts[23] and thus that he was 'knowingly a party to the carrying on of the business' in the statutorily offensive manner. The evidence fully warranted the trial judge's conclusion that the CC was 'essentially a family business or a conglomerate of associated family businesses'.

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[20] *Ad Valorem Factors Ltd v Ricketts* [2003] EWCA Civ 1706, [2004] 1 All ER 894 (CA) para 2 per Mummery LJ.
[21] *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 (4) SA 790 (A) at 803H.
[22] *Philotex (Pty) Ltd v Snyman* 1998 (2) SA 138 (SCA) 143F and 142H-I.
[23] *Howard v Herrigel NO* 1991 (2) SA 660 (A) 673I-J.

So too was the corollary, that reckless disregard of corporate form and requirements and accountability pervaded the management of the family business.

[24] There can be no doubt that both Ebrahims were knowingly a party to this style of business: each was independently and both were jointly responsible for it. They worked in close association with each other in running the CC's affairs. Ebrahim senior was the mastermind and guiding hand behind the group of entities. But Ebrahim junior was more than merely a cipher. He was the sole member of the CC, signed the plaintiff's credit application, and remained involved in the practical arrangement of the CC's business. He, too, was knowingly a party to the reckless trading.

[25] This conclusion makes it unnecessary to go further and make a finding as to whether the Ebrahims' conduct also amounted to fraud. It is likewise unnecessary to consider the application of s 65 (abuse of separate juristic personality) and s 63(h) (no accounting officer).

[26] On the facts he rightly found, s 64(1) entrusted the trial judge with a discretion ('a Court may') to make the order sought. No basis has been advanced to suggest that Griesel J's exercise

of this discretion can be impugned. In my view his order was fully warranted.

The challenge to Griesel J's fair-mindedness

[27] It is necessary to note in conclusion that the Ebrahims' attorney clouded the aftermath of the trial by launching a spurious attack on the trial judge's impartiality. In applying for leave to appeal on behalf of the Ebrahims, he claimed that Griesel J 'was biased against them, and [that] they did not have a fair trial'. These submissions were purportedly made 'respectfully and regrettably', but they were as devoid of respect or regret as they were of substance. No portion of the record offers any warrant for them.

[28] In granting leave to appeal, Griesel J gave full and careful consideration to the claims. He found, correctly, that they were without any merit. Yet the Ebrahims' attorney persisted in advancing them in the notice of appeal. When invited during argument to vouch for this, he purported for the first time to disavow the allegations. This shows an insufficient appreciation of the elements of professional conduct. The claims should never have been made.

[29] Indeed, one may respectfully wonder whether they did not contribute to the decision of the trial judge, erring on the side of accommodation, to grant leave to appeal. If so, the trial judge's self-effacement was unwarranted. There is no merit in the appeal, and it must be dismissed with costs.

E CAMERON
JUDGE OF APPEAL

APPEARANCES:

For appellants:	MR Khan of MR Khan & Associates, Cape Town (the written argument having been prepared by BG Atkins) Coetzee's Attorneys, Bloemfontein
For respondent:	R van Helden (advocate) Mallinicks Inc, Cape Town Lovius Block Attorneys, Bloemfontein