

# PIERCING THE VEIL UNDER SECTION 20(9) OF THE COMPANIES ACT 71 OF 2008: A NEW DIRECTION

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## I INTRODUCTION

The separate legal personality of a company is the very foundation on which company law rests. The Companies Act 71 of 2008 ('the Companies Act') has introduced into South African company law, for the first time, a statutory provision permitting inroads to be made into this fundamental principle. Section 20(9) of the Companies Act permits a court to disregard the separate legal personality of a company and to pierce the corporate veil in instances of 'an unconscionable abuse of the juristic personality of the company as a separate entity'.

While this provision is to be welcomed, it does raise many questions and uncertainties. For instance, the section fails to define the term 'unconscionable abuse' and to provide any guidance on the circumstances that constitute an 'unconscionable abuse' of the juristic personality of the company as a separate entity. It is also not clear from a reading of the section whether section 20(9) overrides the common law or the judicial instances of piercing the corporate veil, or whether piercing of the veil must still be regarded as an exceptional remedy to be used only as a last resort, as is the case at common law. Moreover, section 20(9) does not provide guidance in regard to who would constitute an 'interested person' within the scope and ambit of the section.

In the recent case of *Ex parte Gore and Others NNO*<sup>1</sup> ('Gore') the Western Cape High Court, per Binns-Ward J, delivered the first judgment on section 20(9) of the Companies Act. The case dealt with the issue of piercing the corporate veil in the context of company groups. The court applied section 20(9) of the Companies Act to the facts before it and resolved to pierce the corporate veil. In the course of its judgment, the court answered some of the questions set out above, and usefully set

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<sup>1</sup> 2013 (3) SA 382 (WCC).

out some important guidelines in regard to the interpretation and application of section 20(9) of the Companies Act.

The first part of this article will examine some of the guidelines provided by *Gore* for the interpretation of section 20(9) of the Companies Act. It will be argued that the wording and the interpretation of section 20(9) of the Companies Act as decided in *Gore* result in giving courts very wide powers to pierce the corporate veil, which hitherto never existed under the common-law remedy of piercing the corporate veil. Even though some of the questions and uncertainties regarding the interpretation of section 20(9) of the Companies Act may have been addressed in *Gore*, what remains unclear is the general effect of the exercise of this power on the remedy of piercing the corporate veil in South African law.

The second part of this article will argue that, in the light of the extensive powers given to courts to pierce the corporate veil under section 20(9) of the Companies Act, in applying the section it is of fundamental importance that courts do not disregard the separate legal personality of a company too easily, and that they ensure that the correct balance is struck between piercing the corporate veil and upholding the overarching principle of the separate legal personality of a company enshrined in section 19(1) of the Companies Act. As stated above, courts must exercise caution and wisdom to ensure that they do not develop a disproportionate and inappropriate application of the doctrine of piercing the corporate veil in South African law.

Finally, the third and final part of this article will contend that courts must interpret and apply section 20(9) of the Companies Act in a way that results in clarity and simplicity in the statutory doctrine of piercing the corporate veil. Two ways in which this may be done are suggested in the third part of the article.

As the court in *Gore* emphasised, the Companies Act enjoins that its provisions be construed with appropriate regard to section 5(2) of the Companies Act, which provides that, to the extent appropriate, a court interpreting or applying the Companies Act may consider foreign law.<sup>2</sup> Accordingly, where relevant, this article will refer to recent trends in foreign law in regard to the doctrine of piercing the corporate veil that may serve as guidelines to the interpretation and the application of the doctrine in South African law.

<sup>2</sup> *Idem* para 32.

## II INTERPRETATION OF SECTION 20(9) OF THE COMPANIES ACT

Section 20(9) of the Companies Act states:

‘If, on application by an interested person or in any proceedings in which a company is involved, a court finds that the incorporation of the company, any use of the company, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity, the court may—

- (a) declare that the company is to be deemed not to be a juristic person in respect of any right, obligation or liability of the company or of a shareholder of the company or, in the case of a non-profit company, a member of the company, or of another person specified in the declaration; and
- (b) make any further order the court considers appropriate to give effect to a declaration contemplated in paragraph (a).<sup>3</sup>

The language of section 20(9) has undoubtedly been cast in very wide terms, which, as *Gore* remarked, indicate an appreciation by the legislature that the provision would apply in widely varying factual circumstances.<sup>4</sup> Some elements of section 20(9) that illustrate the breadth of the provision are discussed below.

### (a) *Invoking section 20(9) of the Companies Act*

Section 20(9) of the Companies Act may be invoked by means of an application by an interested person (discussed further below). The words ‘or in any proceedings in which a company is involved’ in section 20(9) make it clear that a court may of its own initiative (*mero motu*) pierce the corporate veil. This interpretation of section 20(9) was confirmed in *Gore’s* case.<sup>5</sup> A court may thus disregard the separate legal personality of a company even where the applicant or plaintiff in the matter before it has not requested the court to do so. This already

<sup>3</sup> Confusion may arise as to the reason why the heading of s 163 of the Companies Act reads as follows: ‘Relief from oppressive or prejudicial conduct or from abuse of separate juristic personality of company.’ The reason is that before the Companies Amendment Act 3 of 2011 came into force, the section on abuse of separate juristic personality was located in s 163 of the Companies Act. When the provision was moved by the Companies Amendment Act 3 of 2011 to s 20 of the Companies Act, the legislature inadvertently failed to amend the heading of s 163 of the Companies Act to remove the incorrect reference to the abuse of the separate juristic personality of a company.

<sup>4</sup> *Supra* note 1 para 32.

<sup>5</sup> *Idem* para 35.

illustrates the width of the powers given to the courts under section 20(9) of the Companies Act to pierce the corporate veil.

*(b) Instances in which section 20(9) may be applied*

Under section 20(9) of the Companies Act, the corporate veil will be pierced where a court finds that there was an unconscionable abuse of the juristic personality of the company as a separate entity. In order for section 20(9) of the Companies Act to apply, unconscionable abuse of the juristic personality of a company must occur in any one of three instances: (i) on the incorporation of the company; (ii) as a result of any use of the company as a legal entity; or (iii) as a result of any act by, or on behalf of, the company.

It is clear from the wording of section 20(9) that the provision may be invoked not only where the incorporation of a company constitutes an unconscionable abuse of the juristic personality of the company as a separate entity, but also where a company has initially been legitimately established but is thereafter misused. This position accords with the position at common law. In *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*,<sup>6</sup> the then Appellate Division stated that under the common law, the corporate personality of a company may be disregarded even if the company had been legitimately established and operated but was subsequently misused in a particular instance to perpetrate a fraud, or for a dishonest or improper purpose, and that it is not necessary for the company to have been ‘conceived and founded in deceit’<sup>7</sup> before its corporate personality may be disregarded. In the English case of *Faiza Ben Hashem v Ali Shayif*,<sup>8</sup> Munby J also remarked that a company may be a façade even though it was not originally incorporated with any deceptive intent — the question is whether it is being used as a façade at the time of the relevant transaction.<sup>9</sup>

The word ‘may’ in section 20(9) indicates that courts have a discretion whether to pierce the corporate veil. Thus, even if the requirements of section 20(9) are fulfilled, a court is not obliged to pierce the corporate veil, but has a discretion whether to do so.

*(c) Orders which may be made by a court under section 20(9) of the Companies Act*

If a court finds that there was an unconscionable abuse of the juristic personality of the company as a separate entity, it may declare a

<sup>6</sup> 1995 (4) SA 790 (A).

<sup>7</sup> *Idem* at 804.

<sup>8</sup> [2008] EWHC 2380 (Fam).

<sup>9</sup> *Idem* para 164.

company not to be a juristic person in respect of any rights, obligations or liabilities of the company, or of a shareholder of the company, or, in the case of a non-profit company, a member of the company or of another person specified in the declaration. A court does not have the power to intervene under section 20(9) of the Companies Act where the unconscionable abuse is not in respect of any such right, obligation or liability. In declaring that a company is deemed not to be a juristic person, a court is given a wide discretion by section 20(9)(b) of the Companies Act to make any further orders that it considers appropriate to give effect to such declaration. The court in *Gore* pointed out that an order made in terms of section 20(9)(b) will always have the effect of fixing the right, obligation or liability of the company somewhere else.<sup>10</sup>

This again illustrates the extensive powers conferred by section 20(9) on the courts. As the court in *Gore* commented, section 20(9)(b) gives the courts ‘the very widest of powers to grant consequential relief’.<sup>11</sup>

(d) ‘Interested person’ under section 20(9) of the Companies Act

The application to declare that the company be deemed not to be a juristic person must be brought by an ‘interested person’. This term is not defined in section 20(9) of the Companies Act. In *Gore* the court stated that no mystique should be attached to the term ‘interested person’ and held:

‘The standing of any person to seek a remedy in terms of the provision should be determined on the basis of well-established principle; see *Jacobs en ’n Ander v Waks en Andere* 1992 (1) SA 521 (A), at 533J-534E, and, of course, if the facts happen to implicate a right in the Bill of Rights, section 38 of the Constitution.’<sup>12</sup>

In *Gore* the controllers of various companies in a group had treated the

<sup>10</sup> Supra note 1 para 34.

<sup>11</sup> Ibid. See further F H I Cassim et al *Contemporary Company Law* 2 ed (2012) 62–3.

<sup>12</sup> Idem para 35. Section 38 of the Constitution of the Republic of South Africa, 1996, which deals with the Enforcement of Rights, provides as follows:

‘Anyone listed in this section has the right to approach a competent court, alleging that a right in the Bill of Rights has been infringed or threatened, and the court may grant appropriate relief, including a declaration of rights.

The persons who may approach a court are:

- (a) anyone acting in their own interest;
- (b) anyone acting on behalf of another person who cannot act in their own name;
- (c) anyone acting as a member of, or in the interest of, a group or class of persons;
- (d) anyone acting in the public interest; and
- (e) an association acting in the interest of its members.’

group of companies in a way that had failed to draw a proper distinction between the separate personalities of the constituent members of the group. The court found that the case fell within the ambit of section 20(9) of the Companies Act, and ruled that the impropriety of the controllers of the group had constituted an unconscionable abuse of the juristic personalities of the subsidiary companies as separate entities. As to the question whether the applicants, who were the liquidators of the various companies that had formed part of the group of companies, were ‘interested persons’ under section 20(9) of the Companies Act, the court had no hesitation in finding that the liquidators of the companies had a direct and sufficient interest in the relief sought so as to qualify as ‘interested persons’ under section 20(9) of the Companies Act.<sup>13</sup>

A person who claims relief from a court in respect of any matter must as a general rule establish that he or she has a direct interest in that matter in order to acquire the necessary locus standi to seek relief.<sup>14</sup> In *Jacobs v Waks*<sup>15</sup> the then Appellate Division stated that the direct interest should not be remote, and that it must be a real interest and not an abstract, academic or hypothetical interest.<sup>16</sup>

In a broad sense, ‘every individual has an interest in every suit that is pending, for he may be placed to-morrow in the position of either plaintiff or defendant in a case in which the same principle may be involved’.<sup>17</sup> However, as emphasised in *Dalrymple v Colonial Treasurer*,<sup>18</sup> courts are not constituted for the discussion of academic questions — they require the litigant to have not only an interest, but also an interest that is not too remote.<sup>19</sup> For instance, in *Dalrymple v Colonial Treasurer*,<sup>20</sup> the question before the court was whether taxpayers had a sufficiently close interest in the matter to institute an action where they contended that the executive government had breached a statute (the Members of Parliament Act 12 of 1907) by spending public funds contrary to the provisions of the statute. The applicants contended that it was their right to see that public funds were not expended in contravention of the Members of Parliament Act 1907. The court ruled that a taxpayer who has paid his taxes does not have a right to be

<sup>13</sup> *Gore* supra note 1 para 35.

<sup>14</sup> *Cabinet of the Transitional Government for the Territory of South West Africa v Eins* 1988 (3) SA 369 (A) 388.

<sup>15</sup> 1992 (1) SA 521 (A).

<sup>16</sup> *Idem* at 533–4.

<sup>17</sup> *Dalrymple v Colonial Treasurer* 1910 TS 372 at 390.

<sup>18</sup> *Supra* note 17.

<sup>19</sup> *Idem* at 390. See also *Cabinet of the Transitional Government for the Territory of South West Africa v Eins* supra note 14 at 388.

<sup>20</sup> *Supra* note 17.

consulted in the disposition of those taxes, and if the collected taxes are wrongfully dealt with by the Minister of the Crown, the individual taxpayer's interest in the taxes would be too remote to enable him to summon the Minister before a court to defend his action.

In *Jacobs v Waks*,<sup>21</sup> the court declared that the assessment of whether a litigant's interest in a case qualifies as a direct interest, or whether it is too remote, would always depend on the particular facts of each individual case, and that no definite rule can be laid down.<sup>22</sup>

Applying this declaration to section 20(9) of the Companies Act, each application before the court would necessitate the court's examining whether the interest of the applicant in deeming a company not to be a juristic person is a direct interest that is not too remote, abstract, academic or hypothetical. The fact that no definite rule can be laid down to answer this question means that courts must exercise their own discretion on this issue on a case-by-case basis.

Section 65 of the Close Corporations Act 69 of 1984 ('the Close Corporations Act') permits a court to deem a close corporation not to be a juristic person. Section 20(9) of the Companies Act is worded very similarly to section 65 of the Close Corporations Act, which states as follows:

'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.'

In *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO*,<sup>23</sup> which examined the meaning of the term 'interested person' in the context of section 65 of the Close Corporations Act, the court remarked that the term 'interested person' is not to be interpreted too restrictively, but at the same time it is not to be interpreted too widely so as to include an

<sup>21</sup> *Supra* note 15.

<sup>22</sup> *Idem* at 534. See further *Dalrymple v Colonial Treasurer* *supra* note 17 at 390 and *Director of Education, Transvaal v McCagie and Others* 1918 AD 616 at 627.

<sup>23</sup> 1998 (1) SA 971 (O).

indirect interest.<sup>24</sup> The interest must be material, relevant or direct, and, in particular, it is limited to a financial or monetary interest.<sup>25</sup> The court commented that a creditor of a close corporation, for instance, would be an 'interested person' under section 65 of the Close Corporations Act.<sup>26</sup> The question that arises is whether an applicant under section 20(9) of the Companies Act would, in the light of the interpretation of 'interested person' in the almost identically worded section 65 of the Close Corporations Act, also have to demonstrate that his interest is of a financial or monetary nature.

In *Gore* the court did not explicitly deal with whether an 'interested person' under section 20(9) of the Companies Act must have a financial or monetary interest, nor did the court refer to the interpretation given to the term 'interested person' by *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO*.<sup>27</sup> The court simply approved of and adopted the general principles stated in *Jacobs v Waks*.<sup>28</sup> In the latter case the Appellate Division commented that it is not essential that the interest should be measurable in monetary terms.<sup>29</sup> Interestingly, and perhaps instructively, in *Jacobs v Waks* the court found that the second respondent in that case had a direct interest in the setting aside of certain decisions by the City Council on the ground that his dignitas had been infringed by such decisions. It is arguable that, by implication, *Gore* did not require that an 'interested person' under section 20(9) of the Companies Act must have a financial or monetary interest. This extends the scope of section 20(9) of the Companies Act much more widely than that of section 65 of the Close Corporations Act, where a financial or monetary interest is a requirement. It is debatable whether this is what the court in *Gore* really intended.

On the one hand, it may be contended that owing to the very close similarity in the wording of section 65 of the Close Corporations Act and section 20(9) of the Companies Act, the narrow approach to the interpretation of 'interested person' under section 65 of the Close Corporations Act ought to be adopted to section 20(9) of the Companies Act, and that a requirement of a financial or monetary interest ought also to be imposed under section 20(9) of the Companies Act. On the other hand, it is arguable that the term 'interested person' must be

<sup>24</sup> *Idem* at 986.

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.*

<sup>27</sup> *Supra* note 23.

<sup>28</sup> *Supra* note 15.

<sup>29</sup> *Ibid* at 535. In *Director of Education, Transvaal v McCagie* *supra* note 22 the court also held that the relevant interest need not be a financial or monetary one (at 629).

interpreted in the light of the legislature's intention in the creation of the Close Corporations Act.

Note that, as from 1 May 2011, which is the date when the Companies Act came into force, new close corporations may no longer be formed and companies may not be converted into close corporations. However, existing close corporations may continue to exist indefinitely and will continue to be regulated by the Close Corporations Act.<sup>30</sup> In *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO*<sup>31</sup> it was stated that the objective of establishing a close corporation as an alternative form of business was to create a simpler and less expensive legal form for the single entrepreneur, having regard to the socioeconomic and political importance of small businesses.<sup>32</sup> In a close corporation, ownership and control are not split, as is generally the case in a public company, and companies tend to be larger and more complex than close corporations, and may even be formed for non-profit purposes. On this basis it may be contended that these differences between companies and close corporations justify the imposition of a financial or monetary interest requirement in order to qualify as an interested person in regard to close corporations, but not so in regard to companies.

It is, however, to be noted that the Companies Act does now provide for small owner-managed companies that are akin to close corporations to be run in a simplified and flexible manner. These provisions were presumably inserted in the Companies Act in the light of the policy decision taken not to permit new close corporations to be formed as from 1 May 2011, nor to permit companies from being converted into close corporations as from 1 May 2011, as discussed above. For example, section 57(4) of the Companies Act simplifies the holding of meetings where every shareholder is also a director of the company, by permitting a board meeting and a shareholders' meeting to be rolled into one, and conveniently dispenses with unnecessary compliance with internal formalities in such a company.<sup>33</sup> Another example would be section 57(2) of the Companies Act, which dispenses with the necessity of internal formalities having to be complied with where a profit company has only one shareholder. Similarly, section 57(3) of the Companies Act dispenses with compliance with internal formalities where a profit company has only one director. In addition, companies in which the

<sup>30</sup> Refer to Schedule 3 item 2(1) of the Companies Act.

<sup>31</sup> *Supra* note 23.

<sup>32</sup> *Idem* at 986.

<sup>33</sup> This is subject to certain requirements being fulfilled, as set out in s 57(4) of the Companies Act.

shareholders and directors are the same persons are exempt from having their annual financial statements audited or even independently reviewed.<sup>34</sup> The question thus arises: is it justifiable to apply a liberal approach to the meaning of ‘interested person’ under section 20(9) of the Companies Act in regard to small owner-managed companies that are akin to close corporations, and that may be run in a less expensive and simplified manner, but to apply a stringent approach to the meaning of ‘interested person’ in section 65 of the Close Corporations Act, where a requirement of a financial or monetary interest is imposed?

It is questionable whether it was the intention of *Gore* to extend the scope of section 20(9) of the Companies Act much more widely than that of section 65 of the Close Corporations Act, where a financial or monetary interest is a requirement. It is submitted that the meaning of ‘interested person’ under section 20(9) of the Companies Act ought to be limited to a financial interest. Until this discrepancy is clarified by our courts, it must be remembered that it was emphasised by the Appellate Division in *Jacobs v Waks*<sup>35</sup> that the assessment of whether a litigant’s interest in a case qualifies as a direct interest or whether it is too remote would always depend on the particular facts of each individual case. Thus a court may still, in its discretion, find that on the facts of a particular case before it under section 20(9) of the Companies Act, the absence of a financial or monetary interest by an ‘interested person’ would result in the interest being too remote, and that accordingly a financial or monetary interest would be required.

(e) *Unconscionable abuse*

The Companies Act does not define the term ‘unconscionable abuse’ and provides no guidance on the circumstances that would constitute an unconscionable abuse of the juristic personality of the company. It has been left entirely to the courts to determine the meaning and scope of this term.

The term ‘unconscionable abuse’ is not to be confused with the term ‘onduldbare onreg’, which is translated as ‘unconscionable injustice’ in *Botha v Van Niekerk*.<sup>36</sup> In this case the court stated that it would pierce the corporate veil if the plaintiff has suffered ‘unconscionable injustice’

<sup>34</sup> See s 30(2A) of the Companies Act, which sets out some exceptions to the application of this provision.

<sup>35</sup> *Supra* note 15.

<sup>36</sup> *Botha v Van Niekerk en ’n Ander* 1983 (3) SA 513 (W).

as a result of improper conduct on the part of the defendant.<sup>37</sup> It is submitted that the court in *Gore* was correct in finding that the difference between the terms ‘unconscionable abuse’ in section 20(9) of the Companies Act and ‘unconscionable injustice’ is that ‘unconscionable abuse’ relates to the conduct giving rise to the remedy of piercing the corporate veil, whereas ‘unconscionable injustice’ relates to the consequences of the conduct suffered by the plaintiff.<sup>38</sup>

In *Gore* the court had no hesitation in finding that there was an unconscionable abuse of the juristic personalities of the companies in the group as separate entities. The court found that the improprieties had involved the controllers of the companies treating the group in a way that had not drawn any proper distinction between the separate personalities of the constituent members, and in using the investors’ funds in a manner inconsistent with what had been represented.<sup>39</sup> For instance, funds solicited from investors had been transferred by the controllers of the holding company between the various companies in the group at will, with no regard for the individual identity of the companies concerned. In many instances the documentation purporting to evidence an investment did not identify the company in which the particular investment ostensibly was being made. The invested funds were in fact allocated by the controllers of the group into whichever company they saw fit, which was generally the company in the group that required immediate funds at the time. This occurred without any properly kept accounting records. The court found that the flow of funds within the group appeared to have been materially determined by the need of the controllers of the group to sustain their scheme by finding money to pay out existing investors who wished to withdraw their funds. Accordingly, the court declared that the companies in the group, with the exception of the holding company, were deemed not to be juristic persons in respect of any obligation by such companies to the investors, and that these companies were to be regarded as a single entity by ignoring their separate legal existence and treating the holding company as though it were the only company.

In regard to the meaning of the term ‘unconscionable abuse of the

<sup>37</sup> *Idem* at 525. In *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* supra note 6 at 805, the Appellate Division commented that the test of unconscionable injustice laid down in *Botha v Van Niekerk* supra note 36 for the purposes of determining when to pierce the corporate veil is too narrow and rigid and a more flexible test must be adopted, which would allow the facts of each case ultimately to determine whether the piercing of the corporate veil is called for.

<sup>38</sup> *Gore* supra note 1 para 34n36.

<sup>39</sup> *Idem* para 33.

juristic personality of a company' in section 20(9) of the Companies Act, the court held that these words postulate conduct in relation to the formation and use of companies that is diverse enough to cover all the descriptive terms such as 'sham', 'device', 'stratagem', and 'conceivably much more'.<sup>40</sup> The court thus adopted a very wide interpretation of the words 'unconscionable abuse'.

Not only did *Gore* adopt a very wide interpretation of the words 'unconscionable abuse', but it also set a lower standard of abuse than that required for the piercing of the veil of close corporations under section 65 of the Close Corporations Act. One difference between section 20(9) of the Companies Act and section 65 of the Close Corporations Act is that section 65 deems a close corporation not to be a juristic person in instances of a 'gross abuse' of the juristic personality of the corporation as a separate entity, whereas section 20(9) deems a company not to be a juristic person where there is an 'unconscionable abuse' of the juristic personality of the company as a separate entity. The court found that the words 'gross abuse' in section 65 of the Close Corporations Act have a 'more extreme connotation'<sup>41</sup> than the words 'unconscionable abuse' in section 20(9) of the Companies Act. Thus, in order for the corporate veil of a company to be pierced under section 20(9) of the Companies Act, a lower standard of abuse would need to be proved compared to the level of abuse required for the corporate veil of a close corporation to be pierced under section 65 of the Close Corporations Act.

It is questionable why the legislature chose not to use the words 'gross abuse' in section 20(9) of the Companies Act, despite the section being so similarly worded to section 65 of the Close Corporations Act in nearly every other respect. It is also questionable why the court in *Gore* postulated a lower standard of abuse for section 20(9) of the Companies Act compared to section 65 of the Close Corporations Act, when in general both companies and close corporations are statutorily formed and registered for the purpose of, and benefit of, limited liability. One might argue that on *Gore's* interpretation of the pivotal words 'unconscionable abuse', just about any abuse of the juristic personality of a company would be unconscionable. It is debatable whether too low a level or threshold of abuse has been set by *Gore*, particularly in the light

<sup>40</sup> *Idem* para 34.

<sup>41</sup> *Ibid.* For a discussion of the meaning and examples of the term 'gross abuse', see *Haygro Catering BK v Van der Merwe en Andere* 1996 (4) SA 1063 (C); *TJ Jonck BK h/a Bothaville Vleismark v Du Plessis NO* supra note 23; *Airport Cold Storage (Pty) Ltd v Ebrahim and Others* 2008 (2) SA 303 (C); Cassim et al op cit note 11 at 60–2; and Rehana Cassim 'Piercing the corporate veil: Unconscionable abuse under the Companies Act 71 of 2008' August 2012 *De Rebus* 22 at 23–4.

of the fact that, as previously discussed, the Companies Act now provides for small owner-managed companies that are akin to close corporations to be run more simply.

In *Gore* the court stated further that section 20(9) of the Companies Act brings about a remedy that may be provided ‘whenever the illegitimate use of the concept of juristic personality adversely affects a third party in a way that reasonably should not be countenanced’.<sup>42</sup> The broad interpretation given to the term ‘unconscionable abuse’ by *Gore*, together with the remedy of piercing the corporate veil being available whenever the illegitimate use of the company’s separate legal personality affects one in a way that should not reasonably be countenanced, make it clear that the legal bases upon which courts have hitherto been prepared to pierce the corporate veil under the common law have now been considerably extended under section 20(9) of the Companies Act.<sup>43</sup>

By way of illustration, the question before the Supreme Court of the United Kingdom in the recent case of *VTB Capital plc v Nutritek International Corp*<sup>44</sup> was whether, if a person used a puppet<sup>45</sup> company to enter into a contract with a third party in order to perpetrate a fraud on that third party, the corporate veil may be pierced with the consequence that the puppeteer would be treated as a party to the contract. The Supreme Court refused to pierce the corporate veil in this instance. The court held that to do so would amount to an extension to the circumstances in which the corporate veil has been traditionally pierced because it would lead to the person controlling the company being held liable as if he had been a co-contracting party with the company concerned to a contract to which the company and not he was a party.<sup>46</sup>

However, Lord Neuberger, who wrote the unanimous judgment in this case on the issue of piercing the corporate veil, observed that the interposition of pertinent statutory provisions could determine a different conclusion on the question of whether, and in which circumstances, a court could pierce the corporate veil.<sup>47</sup> In *Gore*, commenting on this statement made by Lord Neuberger, the court remarked that section

<sup>42</sup> Supra note 1 para 34.

<sup>43</sup> See *Gore* idem para 33.

<sup>44</sup> [2013] 2 AC 337.

<sup>45</sup> Reference to the word ‘puppet’ means that the company is under a person’s control.

<sup>46</sup> Supra note 44 para 132. The court of first instance (the Chancery Division) (in *VTB Capital plc v Nutritek International Corp* [2011] EWHC 3107 (Ch)) did not pierce the corporate veil, and the Court of Appeal (in *VTB Capital plc v Nutritek International Corp* [2012] 2 Lloyd’s Rep 313; [2012] 2 BCLC 437; [2012] 2 CLC 431) again refused to pierce the corporate veil.

<sup>47</sup> *VTB Capital plc v Nutritek International Corp* supra note 44 para 130.

20(9) of the Companies Act is indeed a manifestation of such provision.<sup>48</sup> While the court in *Gore* stated that it was not necessary to determine the question, it did nevertheless comment that it was not clear that the United Kingdom Supreme Court would have come to the same conclusion had a statutory provision akin to section 20(9) of the Companies Act been applicable in English law.<sup>49</sup> It seems quite possible that if South African courts were to determine the same question that was before the court in *VTB Capital plc v Nutritek International Corp*,<sup>50</sup> in the light of and in reliance on section 20(9) of the Companies Act, they might well come to a different conclusion on whether the corporate veil could be pierced in this instance. As the court in *Gore* confirmed and stated above, the ambit of section 20(9) appears indeed to have broadened the bases upon which South African courts have hitherto under the common law been prepared to grant relief that entails disregarding corporate personality.<sup>51</sup>

(f) *Not a remedy of last resort*

As discussed further in paragraph IV below, there is uncertainty and much confusion in regard to the doctrine of piercing the corporate veil under the common law. One manifestation of this uncertainty emanates from the question whether piercing the corporate veil is a remedy of last resort under the common law.

In *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*<sup>52</sup> the Appellate Division remarked that if the facts of a particular case justify piercing of the corporate veil, the existence of another remedy should not in principle serve as a bar to a court piercing the corporate veil.<sup>53</sup> The Appellate Division stated further that the existence of another remedy, or the failure to pursue one that was available, would be a relevant factor when policy considerations come into play, but it is not of overriding importance.<sup>54</sup>

Subsequent decisions at common law did not favour this view. In *Hülse-Reutter v Gödde*,<sup>55</sup> the Supreme Court of Appeal adopted a stricter approach in this respect and stated:

<sup>48</sup> Supra note 1 para 24.

<sup>49</sup> Ibid.

<sup>50</sup> Supra note 44.

<sup>51</sup> Supra note 1 para 33.

<sup>52</sup> Supra note 6.

<sup>53</sup> Idem at 805.

<sup>54</sup> Ibid.

<sup>55</sup> 2001 (4) SA 1336 (SCA).

‘The very exceptional nature of the relief which the respondent seeks against the appellants requires, in the circumstances of the present case, that he should have no other remedy.’<sup>56</sup>

In *Gore* the court stated, obiter, that this assertion of the Supreme Court of Appeal in *Hülse-Reutter v Gödde*<sup>57</sup> has been misunderstood to imply that the corporate veil should not be pierced if the claimant has an alternative remedy, but in fact it goes no further than to state that, depending on the facts of a given case, the existence of an alternative remedy may be a relevant consideration.<sup>58</sup>

In *Amlin (SA) Pty Ltd v Van Kooij*,<sup>59</sup> however, the Cape Provincial Division was emphatic in stating that piercing the corporate veil must be used as a remedy of last resort. Dlodlo J stated:

‘I accept that “opening the curtains” or piercing the veil is rather a drastic remedy. For that reason alone it must be resorted to rather sparingly and indeed as the very last resort in circumstances where justice will not otherwise be done between two litigants. It cannot, for example, be resorted to as an alternative remedy if another remedy on the same facts can successfully be employed in order to administer justice between the parties.’<sup>60</sup>

In *Gore* the Western Cape High Court clearly acknowledged that under the common law a judicial philosophy exists that the separate legal personality of a company should be disregarded only in exceptional circumstances and as a last resort.<sup>61</sup>

In the English case of *Prest v Petrodel Resources Limited*,<sup>62</sup> the Supreme Court also remarked that the power to pierce the corporate veil is to be exercised when ‘all other, more conventional, remedies have proved to be of no assistance’.<sup>63</sup> The Supreme Court in this case adopted a conservative approach towards the doctrine of piercing the corporate veil and commented pertinently that ‘if it is not necessary to pierce the corporate veil, it is not appropriate to do so, because on that footing there is no public policy imperative which justifies that course’.<sup>64</sup>

<sup>56</sup> *Idem* para 23.

<sup>57</sup> *Supra* note 55.

<sup>58</sup> *Supra* note 1 para 34n38.

<sup>59</sup> 2008 (2) SA 558 (C).

<sup>60</sup> *Idem* para 23.

<sup>61</sup> *Supra* note 1 para 27. See further *Airport Cold Storage (Pty) Ltd v Ebrahim* *supra* note 41 para 9 and *Al-Kharafi & Sons v Pema and Others* NNO 2010 (2) SA 360 (W) paras 36–7.

<sup>62</sup> *Prest v Petrodel Resources Limited* [2013] 2 AC 415.

<sup>63</sup> *Idem* para 62.

<sup>64</sup> *Idem* para 35.

The question thus arises whether the same common-law principle is to be applied to section 20(9) of the Companies Act: that is, whether section 20(9) is to be applied only when all other, more conventional remedies, are of no assistance.

*Gore* is authority for the view that the answer to this question is in the negative. The court remarked that the unqualified availability of the remedy under section 20(9) militates against an approach that the remedy should be granted only in the absence of any alternative remedy.<sup>65</sup> It is submitted that the court's interpretation of section 20(9) is in this respect correct. Binns-Ward J held:

'The newly introduced statutory provision affords a firm, albeit very flexibly defined, basis for the remedy, which will inevitably operate, I think, to erode the foundation of the philosophy that piercing the corporate veil should be approached with an *à priori* diffidence. By expressly establishing its availability simply when the facts of a case justify it, the provision detracts from the notion that the remedy should be regarded as exceptional, or "drastic".'<sup>66</sup>

It is submitted that this represents a new direction and a sharp shift in thinking in regard to the remedy of piercing the corporate veil. It has the implication that in the event of a court having the option of applying a remedy to the facts before it that would result in the separate legal personality of a company being upheld, the court may nevertheless choose to pierce the corporate veil and disregard a company's separate legal personality under section 20(9) of the Companies Act. This also brings the position under section 20(9) of the Companies Act more into line with the dicta expressed by the Appellate Division in *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*,<sup>67</sup> that piercing the corporate veil is not a remedy of last resort.

### III ACHIEVING A BALANCE IN APPLYING SECTION 20(9) OF THE COMPANIES ACT

On the question of whether section 20(9) has replaced the common law on piercing the corporate veil, in *Gore* it was held that there is no express intention to this effect (as is seen for instance in section 165(1)<sup>68</sup> of the Companies Act) but, equally, no express indication that the intention is

<sup>65</sup> Supra note 1 para 34. See further Cassim et al op cit note 11 at 58.

<sup>66</sup> Ibid.

<sup>67</sup> Supra note 6.

<sup>68</sup> Section 165(1) of the Companies Act concerns derivative actions. The provision expressly states that any right at common law of a person other than a company to bring or

not to displace the common law (as is seen in section 161(2)(b)<sup>69</sup> of the Companies Act).<sup>70</sup> In the light of the fact that there are no set categories of instances in which a court will pierce the corporate veil at common law<sup>71</sup> and the ‘elusiveness of a convincing definition of the pertinent common-law principles’,<sup>72</sup> the court came to the conclusion that it would be appropriate to regard section 20(9) of the Companies Act as supplemental to the common law, rather than substitutive.<sup>73</sup> Thus where the requirements of section 20(9) are not fulfilled and the section may not be relied upon, the common-law remedy of piercing the veil would still be applicable. The principles developed at common law with regard to piercing the corporate veil would no doubt serve as useful guidelines for interpreting section 20(9) of the Companies Act.

It is submitted that one particular important common-law principle which must serve as a guideline to the court in applying section 20(9) of the Companies Act is that which arises from the leading case of *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*, where Smalberger JA held:<sup>74</sup>

‘It is undoubtedly a salutary principle that our Courts should not lightly disregard a company’s separate personality, but should strive to give effect to and uphold it. To do otherwise would negate or undermine the policy and principles that underpin the concept of separate corporate personality and the legal consequences that attach to it. But where fraud, dishonesty or other improper conduct (and I confine myself to such situations) 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

prosecute any legal proceedings on behalf of that company is abolished, and the rights in s 165 of the Companies Act are in substitution for any such abolished right.

<sup>69</sup> Section 161(2)(b) concerns remedies which are available to protect the rights of the securities holders. The provision states that the right to apply to a court in terms of s 161 is in addition to any other remedy available to a securities holder in terms of the Companies Act or in terms of the common law, subject to the Companies Act. For a further example, see s 20(8) of the Companies Act, which states that s 20(7), concerning the Turquand Rule, is to be construed concurrently with, and not in substitution for, any relevant common-law principle relating to the presumed validity of the actions of a company in the exercise of its powers.

<sup>70</sup> Supra note 1 para 31.

<sup>71</sup> See *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* supra note 6 where the Appellate Division implied that we do not have a categorising approach to piercing the veil in South African law.

<sup>72</sup> *Gore* supra note 1 para 34.

<sup>73</sup> *Ibid.*

<sup>74</sup> Supra note 6.

balanced against policy considerations which arise in favour of piercing the corporate veil. . . .<sup>75</sup>

This balancing approach laid down by the Appellate Division in *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* is modelled on the United States case of *Glazer v Commission on Ethics for Public Employees*,<sup>76</sup> where the Supreme Court of Louisiana stated that the policies behind the recognition of a separate corporate existence must be balanced against the policies justifying piercing.<sup>77</sup> The balancing approach emphasises the importance of a company's separate legal personality and requires a court to balance the need to preserve a company's separate legal personality against policy considerations which arise in favour of piercing the corporate veil. In *Gore*, Binns-Ward J also endorsed the balancing approach in the context of piercing the corporate veil:

'In my view the determination to disregard the distinctness provided in terms of a company's separate legal personality appears in each case to reflect a policy-based decision resultant upon a weighing by the court of the importance of giving effect to the legal concept of juristic personality, acknowledging the material practical and legal considerations that underpin the legal fiction, on the one hand, as against the adverse moral and economic effects of countenancing an unconscionable abuse of the concept by the founders, shareholders, or controllers of a company, on the other.'<sup>78</sup>

Simply put, the court stated that in determining whether to pierce the corporate veil, one must weigh up or balance the importance of giving effect to the separate legal personality of a company against the adverse moral and economic effects of tolerating an unconscionable abuse of the juristic personality of the company.

It is clear from the wide interpretation given by the court in *Gore* to section 20(9) of the Companies Act, as discussed above, that the power of courts to pierce the corporate veil of companies has now increased considerably. Not only is the level of abuse required in order for section 20(9) to be applicable far lower than that required under section 65 of the Close Corporations Act, but, as reasoned in *Gore*, section 20(9) is to

<sup>75</sup> *Idem* at 803. See also *Die Dros (Pty) Ltd and Another v Telefon Beverages CC and Others* 2003 (4) SA 207 (C) para 23; *Al-Kharafi & Sons v Pema* supra note 61 para 37; and *Rees and Others v Harris and Others* 2012 (1) SA 583 (GSJ) para 15.

<sup>76</sup> So 2d 752 (La 1983).

<sup>77</sup> *Idem* at 757.

<sup>78</sup> *Supra* note 1 para 29.

be regarded neither as an exceptional remedy nor as a remedy of last resort. A concern arises whether South African courts would, in the light of their new powers under section 20(9) of the Companies Act, disregard the corporate veil too lightly. Will we see in South African law a development of a disproportionate application of the doctrine of piercing the corporate veil?

As the court in *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*<sup>79</sup> emphasised, if the separate legal personality of a company is too lightly disregarded by courts, this would negate and undermine the policy and principles that underpin the concept of separate corporate personality and the legal consequences that attach thereto.<sup>80</sup> The separate legal personality of a company is soundly affirmed in section 19(1)(b) of the Companies Act, which states that, from the date and time that the incorporation of a company is registered, the company has all the legal powers and capacity of an individual.<sup>81</sup> It would be regrettable if courts were to make undue incursions into this fundamental statutory provision, or the overarching principles laid down in *Salomon v A Salomon and Co Ltd*<sup>82</sup> (*Salomon v Salomon*) that a company is a separate legal person independent and distinct from its shareholders and directors.<sup>83</sup> Lord Templeman referred to the principle in *Salomon v Salomon* as the ‘unyielding rock’<sup>84</sup> on which company law is constructed, and on which ‘complicated arguments’ may in the end become ‘shipwrecked’.<sup>85</sup> Notably, in the seminal case of *Dadoo Ltd v Krugersdorp Municipal Council*<sup>86</sup> Innes CJ held that

‘[t]his conception of the existence of a company as a separate entity distinct from its shareholders is no merely artificial and technical thing. It is a matter of substance’.<sup>87</sup>

<sup>79</sup> Supra note 6.

<sup>80</sup> Idem at 803. See further *Die Dros (Pty) Ltd v Telefon Beverages CC* supra note 75 para 23; *Ebrahim and Another v Airport Cold Storage (Pty) Ltd* 2008 (6) SA 585 (SCA) para 22; *Al-Kharafi & Sons v Pema* supra note 61 para 37; and *Rees v Harris* supra note 75 para 15.

<sup>81</sup> This applies except to the extent that a juristic person is incapable of exercising any such power or having any such capacity, or except to the extent that the company’s Memorandum of Incorporation provides otherwise (s 19(1)(b)(i) and (ii)).

<sup>82</sup> [1897] AC 22 (HL).

<sup>83</sup> As Lord Halsbury LC in *Salomon v Salomon* stated, a legally incorporated company ‘must be treated like any other independent person with its rights and liabilities appropriate to itself . . . whatever may have been the ideas or schemes of those who brought it into existence’ (supra note 82 at 30–1).

<sup>84</sup> Lord Templeman ‘Company law lecture – Forty years on’ (1990) 11 *The Company Lawyer* 10 at 10.

<sup>85</sup> Ibid.

<sup>86</sup> 1920 AD 530.

<sup>87</sup> Idem at 550.

In *Prest v Petrodel Resources Limited*,<sup>88</sup> the United Kingdom Supreme Court recently remarked that the separate personality of a company is sometimes described as a fiction, and in a sense it is, but this fiction is the whole foundation of company law.<sup>89</sup>

In order to ensure that courts do not pierce the corporate veil too lightly, it is submitted that, in exercising their discretion whether to apply section 20(9), courts must carefully apply the balancing approach stated in *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*<sup>90</sup> and *Gore*<sup>91</sup> before piercing the corporate veil and deeming a company not to be a juristic person. Courts must apply their discretion cautiously and wisely and with due consideration to both sides of the balancing equation before piercing the corporate veil under section 20(9) of the Companies Act.

A trend is discernible from recent judgments of the United Kingdom, which is that the courts are exercising much caution and restraint in piercing the corporate veil.<sup>92</sup> South African courts have, however, generally tended to adopt a discernibly more liberal approach to piercing the corporate veil than the English courts.<sup>93</sup> As the Supreme Court of Appeal in *Ebrahim v Airport Cold Storage (Pty) Ltd*<sup>94</sup> observed, in commenting on the application of section 64(1) (personal liability in

<sup>88</sup> Supra note 62. See also *The Shipping Corporation of India Ltd v Evdomon Corporation and Another* 1994 (1) SA 550 (A) 565–6.

<sup>89</sup> *Prest v Petrodel Resources Limited* supra note para 8.

<sup>90</sup> Supra note 6 at 803.

<sup>91</sup> Supra note 1 para 29.

<sup>92</sup> See, for example, the judgments in *Faiza Ben Hashem v Ali Shayif* supra note 8 which crystallised various grounds upon which the corporate veil will be pierced, a case regarded as a leading authority on piercing the corporate veil in the UK; the respective judgments of the Chancery Division, Court of Appeal and the Supreme Court in *VTB Capital plc v Nutritek International Corp* supra note 46; *VTB Capital plc v Nutritek International Corp* supra note 46 and *VTB Capital plc v Nutritek International Corp* supra note 44; and *Prest v Petrodel Resources Limited* supra note 62. The issue before the Supreme Court in *Prest v Petrodel Resources Limited* was whether a number of properties belonging to the Petrodel Group which were wholly owned by Michael Prest (the husband) could be transferred to his wife in the context of divorce proceedings between them, given that the properties legally belonged not to the husband but to his companies. The court found that, for reasons of wealth protection and avoidance of tax, the legal interest in the properties had been vested in the companies a long time before the marriage had dissolved. Accordingly, the court found that the doctrine of piercing the corporate veil was not applicable because the husband's actions did not conceal or evade any legal obligation to his wife, nor was he concealing or evading the law in relation to the distribution of assets of the marriage upon its dissolution. However, the UK Supreme Court did find in favour of the wife in this matter on another ground: that is, that in the particular circumstances of the case, the properties vested in the companies were held by the husband's companies on trust for him and they were accordingly properties to which the husband was entitled, either in possession or reversion.

<sup>93</sup> See *Gore* supra note 1 para 27.

<sup>94</sup> Supra note 80.

regard to conducting business recklessly or for fraudulent purposes) and section 65 of the Close Corporations Act, '[i]n 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, the jurisprudence of this court evidences claimants' spirited reliance on the provision'.<sup>95</sup> It is submitted that this spirited reliance by applicants on piercing the corporate veil may well increase in the light of section 20(9) of the Companies Act, but that courts must give due consideration to balancing the need to preserve a company's separate legal personality against policy considerations which arise in favour of piercing the corporate veil, and refrain from piercing the corporate veil too lightly.

It is instructive that in Brazil, which has various statutory provisions authorising the court to pierce the corporate veil, it is now widely agreed that there has been a disproportionate and inappropriate application of the doctrine of piercing the corporate veil. Piercing the corporate veil in Brazil is statutorily provided for in Article 50 of the Brazilian Civil Code (Law Number 10406 of 2002), which states that if there is a deviation of a company's purpose<sup>96</sup> or the commingling of assets<sup>97</sup> caused by the abuse of its legal entity status by one of its members or managers, the court may consider such partner or manager personally liable without limitation (including personal property) for the company's obligations and debts. Piercing of the corporate veil is also statutorily provided for in the Brazilian Competition Law,<sup>98</sup> Consumer Protection Code,<sup>99</sup> and Envi-

<sup>95</sup> *Idem* para 22.

<sup>96</sup> Deviation of the company's purpose in this context occurs when the truth is distorted to use a company for purposes other than those for which it was established, causing harm to a third party for the benefit of oneself or another (see Luciana Bassani & Rinúccia Faria La Ruina 'Piercing the corporate veil' *Danneman Siemsen News* March/May 2011, available at [http://www.dannemann.com.br/site.cfm?app=show&dsp=dsnews\\_201103\\_4&pos=5.98&lng=en](http://www.dannemann.com.br/site.cfm?app=show&dsp=dsnews_201103_4&pos=5.98&lng=en), accessed on 16 August 2013).

<sup>97</sup> Commingling of assets occurs when funds of the company are misused, for example where corporate funds are used to pay personal debts (see Alan R Palmiter *Corporations* 7 ed (2012) 32–3).

<sup>98</sup> Article 34 of the Brazilian Competition Law (Law Number 12529/2012, effective from 30 May 2012) states: 'The corporate entity may be disregarded in case of violation of the economic order, upon the occurrence of abuse of rights, abuse of powers, violation of law, tort, or violation of the bylaws or the articles of association', and further that '[t]he piercing of the corporate veil also may be ordered upon the occurrence of bankruptcy, insolvency, closure, or inactivity of the corporate entity resulting from mismanagement'.

<sup>99</sup> Article 28 of the Brazilian Consumer Protection Code (Law Number 8078/90 of 11 September 1990) states:

'The court may order the piercing of the corporate veil when, to the detriment of the end consumer, there is abuse of rights, abuse of powers, violation of the law, tort, or violation of the bylaws or the articles of association. The piercing of the corporate veil may also be ordered upon the

ronmental Law.<sup>100</sup> However, the doctrine of piercing the corporate veil in Brazil is thought to be treated by the Brazilian courts in a 'broad, superficial and sparse manner'.<sup>101</sup> It seems that an increasing number of courts in Brazil are piercing the corporate veil,

'without discernment and observation of the legal requirements. . . . The exception has become the rule, defying the limited liability principle and corporate autonomy, which for centuries have enabled and fostered business activity'.<sup>102</sup>

The excessive piercing of the corporate veil by Brazilian courts has entailed the invalidation of the company's corporate entity and the limitation of liability, principles which are both duly recognised by the Brazilian legal system.<sup>103</sup>

Brazil recently introduced into law a new Bill (Bill Number 3401/2008 of 24 April 2008) ('Bill 3401/2008') to regulate the procedure under which a court may pierce the corporate veil. The rationale behind the introduction of Bill 3401/2008, as stated in the Bill itself, is that it is widely agreed that there has been a disproportionate and inappropriate application of the doctrine of piercing the corporate veil.<sup>104</sup> Bill 3401/2008 aims to prevent a misuse of the doctrine of piercing the corporate veil and to safeguard certain principles recognised by the federal Constitution of Brazil. It also aims to establish a specific judicial procedure for piercing the corporate veil, in compliance with the constitutional rights of the due process of law, full defence, and use of the adversary system.<sup>105</sup> For instance, Article 3 of Bill 3401/2008 provides that prior to deciding on whether to order the liability of members, founders, partners, or managers for obligations undertaken by the corporate entity, a court must establish the adversarial process, allowing such members, founders, partners, or managers to exercise their right of full defence.

occurrence of bankruptcy, insolvency, closure, or inactivity of the corporate entity resulting from mismanagement.'

Section 5 of Article 28 states: 'The corporate entity also may be disregarded whenever the separation of its assets constitutes, by any means whatsoever, an obstacle to indemnification for damage caused to end consumers.'

<sup>100</sup> Article 4 of the Brazilian Environmental Law (Law Number 9605/98 of 12 February 1998) provides that '[t]he corporate entity may be disregarded whenever the separation of its assets constitutes an obstacle to indemnification for damage caused to the environment'.

<sup>101</sup> Felipe Toscano 'Piercing the corporate veil under Brazilian law' (2012) 34 *The Comparative Law Yearbook of International Business* 323 at 339.

<sup>102</sup> Bassani & La Ruina *op cit* note 96.

<sup>103</sup> Toscano *op cit* note 101 at 329.

<sup>104</sup> See the justification for Bill 3401/2008 set out in the Bill.

<sup>105</sup> See Toscano *op cit* note 101 at 339.

It would be regrettable if a similar situation which has arisen in Brazil were to arise in South African law in regard to piercing the corporate veil of companies. It is submitted that, in exercising its discretion and powers to pierce the corporate veil under section 20(9) of the Companies Act, South African courts must take pains to ensure that such a situation does not arise and that courts do not develop a disproportionate or inappropriate application of the doctrine of piercing the corporate veil.

#### IV CLARITY AND SIMPLICITY

There exists in South African common law an uncertainty and a high level of confusion in regard to the doctrine of piercing the corporate veil. In *Gore* the court stated that there are no clearly determinable principles in regard to the grounds on which courts will pierce the corporate veil.<sup>106</sup> The court agreed with the statements by Smalberger JA in *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*<sup>107</sup> that '[t]he law is far from settled with regard to the circumstances in which it would be permissible to pierce the corporate veil'.<sup>108</sup>

This uncertainty and confusion in regard to the doctrine of piercing the corporate veil is shared by courts in the United Kingdom. For example, Lord Neuberger of the Supreme Court held in *VTB Capital plc v Nutritek International Corp*<sup>109</sup> in regard to the doctrine of piercing the veil, that 'the precise nature, basis, and meaning of the principle are all somewhat obscure, as are the precise nature of circumstances in which the principle can apply'.<sup>110</sup> In *Prest v Petrodel Resources Limited*,<sup>111</sup> commenting on the question of the circumstances when the corporate veil would be pierced, the Supreme Court asserted that 'the question is heavily burdened by authority, much of it characterised by incautious dicta and inadequate reasoning'.<sup>112</sup> After surveying the authorities on the doctrine of piercing the corporate veil, the Supreme Court came to the conclusion that the law relating to the doctrine is unsatisfactory and confused, and found that it was impossible to discern 'any coherent

<sup>106</sup> Supra note 1 para 21.

<sup>107</sup> Supra note 6.

<sup>108</sup> Idem at 802. See further *Airport Cold Storage (Pty) Ltd v Ebrahim* supra note 41 para 9 and *Rees v Harris* supra note 75 para 14.

<sup>109</sup> Supra note 44.

<sup>110</sup> Idem para 123.

<sup>111</sup> Supra note 62.

<sup>112</sup> Idem para 19.

approach, applicable principles, or defined limitations to the doctrine'.<sup>113</sup>

In the United States of America, piercing the corporate veil is the most litigated issue in corporate law, and it occurs more frequently in that country than anywhere else in the world.<sup>114</sup> Yet the doctrine has been criticised strongly by the courts. For instance, in *Allied Capital Corp v GC-Sun Holdings LP*,<sup>115</sup> the Delaware Court of Chancery remarked that the doctrine of piercing the corporate veil has been 'rightfully criticized for its ambiguity and randomness'<sup>116</sup> and that its application 'yield[s] few predictable results'.<sup>117</sup> Legal writers in the United States have also described judicial decisions to pierce the corporate veil as confusing. For instance, Easterbrook and Fischel have bitingly commented as follows:

“Piercing” seems to happen freakishly. Like lightning, it is rare, severe, and unprincipled. There is a consensus that the whole area of limited liability, and conversely of piercing the corporate veil, is among the most confusing in corporate law.<sup>118</sup>

The lack of a coherent principle in the application of the doctrine of piercing the corporate veil has been commented on in Australian law as well.<sup>119</sup> For example, in *Briggs v James Hardie & Co Pty Ltd*,<sup>120</sup> Rogers AJA in the New South Wales Court of Appeal commented as follows:

‘[T]here is no common, unifying principle, which underlies the occasional decision of the courts to pierce the corporate veil. Although an ad hoc explanation may be offered by a court which so

<sup>113</sup> *Idem* para 64.

<sup>114</sup> Empirical evidence in the USA has documented veil piercing as the most litigated issue in company law. See Robert B Thompson ‘Piercing the corporate veil: An empirical study’ (1991) 76 *Cornell LR* 1036 at 1036; Robert B Thompson ‘Piercing the veil: Is the common law the problem?’ (2005) 37 *Connecticut LR* 619 at 619; and *Prest v Petrodel Resources Limited* supra note 62 paras 76–7. Yet the US courts do not generally pierce the corporate veil so as to remove limited liability in the case of a public company, nor do they do so as a matter of routine in private companies (see Paul L Davies & Sarah Worthington *Gower and Davies’ Principles of Modern Company Law* 9 ed (2012) 223).

<sup>115</sup> A 2d 1020 (Del Ch, 2006).

<sup>116</sup> *Idem* at 1042.

<sup>117</sup> *Idem* at 1043. See further Franklin A Gevurtz *Corporation Law* 2 ed (2000) 69–72 for a discussion of some of the reasons for the confusion in the doctrine of piercing the corporate veil in the USA.

<sup>118</sup> Frank H Easterbrook & Daniel R Fischel ‘Limited liability and the corporation’ (1985) 52 *University of Chicago LR* 89 at 89. See further the authorities cited in *Allied Capital Corporation v GC-Sun Holdings LP* supra note 115 at 1042–3.

<sup>119</sup> See Ian M Ramsay & David B Noakes ‘Piercing the corporate veil in Australia’ (2001) 19 *Company and Securities LJ* 250.

<sup>120</sup> (1989) 16 NSWLR 549.

decides, there is no principled approach to be derived from the authorities.<sup>121</sup>

In a similar vein, the New Zealand Court of Appeal in *Attorney-General v Equiticorp Industries Group Ltd (In Statutory Management)*<sup>122</sup> remarked that

“to lift the corporate veil” . . . is not a principle. It describes the process, but provides no guidance as to when it can be used’.<sup>123</sup>

It is clear that, in South Africa, the United Kingdom, the United States and other leading jurisdictions, the doctrine of piercing the corporate veil is regarded as confusing and uncertain.<sup>124</sup> It is submitted that, in the light of the confusion and uncertainty in the common law on the application of the doctrine of piercing the corporate veil, courts must strive to clarify the doctrine of piercing the corporate veil in South African law. As the United Kingdom Supreme Court held in *Prest v Petrodel Resources Limited*,<sup>125</sup> it is important to maintain clarity and simplicity in piercing the corporate veil, and if the doctrine of piercing the corporate veil is to exist, ‘the circumstances in which it can apply must be limited and as clear as possible’.<sup>126</sup> It is submitted that in interpreting and applying section 20(9) of the Companies Act, courts must endeavour to develop the statutory doctrine of piercing the corporate veil in a way that will maintain clarity and simplicity, so as to demystify the confusion which exists in the common law. Two ways in which the courts may do so are discussed below.

#### (a) *Avoiding the use of metaphors*

One way in which to demystify the confusion and uncertainty surrounding the doctrine of piercing the corporate veil would be for courts to avoid the use of metaphors and derogatory descriptive terms in their judgments. As discussed, *Gore* asserted that the words ‘unconscionable abuse of the juristic personality of a company’ used in section 20(9) of

<sup>121</sup> *Idem* at 567. See also *Idoport Pty Ltd v National Australia Bank Ltd* [2004] NSWSC 695 para 144.

<sup>122</sup> [1996] 1 NZLR 528.

<sup>123</sup> *Idem* at 541.

<sup>124</sup> It has been suggested that a reason for the confusion and uncertainty is that cases on piercing the corporate veil tend to be inherently fact-specific and subject to individual interpretation, which often results in the absence of clarity. See Jason Harris & Anil Hargovan ‘Corporate groups: The intersection between corporate and tax law: *Commissioner of Taxation v BHP Billiton Finance Ltd*’ (2010) 32 *Sydney LR* 723 at 726.

<sup>125</sup> *Supra* note 62.

<sup>126</sup> *Idem* para 67.

the Companies Act postulate conduct in relation to the formation and use of companies which is diverse enough to cover all the descriptive terms such as sham, device, stratagem, and conceivably much more.<sup>127</sup> In *VTB Capital plc v Nutritek International Corp*,<sup>128</sup> Lord Neuberger of the United Kingdom Supreme Court questioned the usefulness of applying words such as façade, sham, mask, cloak, and device, and stated that while such words may be useful metaphors

‘such pejorative expressions are often dangerous, as they risk assisting moral indignation to triumph over legal principle, and, while they may enable a court to arrive at a result which seems fair in the case in question, they can also risk causing confusion and uncertainty in the law’.<sup>129</sup>

In *Prest v Petrodel Resources Ltd*<sup>130</sup> too, the United Kingdom Supreme Court remarked that the use of pejorative expressions masks the absence of rational analysis and should be avoided.<sup>131</sup>

These views expressed by the United Kingdom Supreme Court resonate with the well-known and oft-quoted remark of Justice Cardozo as early as 1926 in the United States case of *Berkey v Third Ave. Ry. Co.*<sup>132</sup> that veil piercing is ‘enveloped in the mists of metaphor’.<sup>133</sup> Justice Cardozo cautioned that ‘metaphors in law are to be narrowly watched, for starting as devices to liberate thought, they end often by enslaving it’.<sup>134</sup> The reason for this could be that these metaphors tend to describe the results without explaining the reasons for the decisions.<sup>135</sup> In a similar vein, in the United States case of *Glazer v Commission on Ethics for Public Employees*,<sup>136</sup> the court proclaimed that the courts often pierce the corporate veil by saying simply that the corporation is the ‘instrumentality’ or ‘alter ego’ of the individual shareholder, ‘without adequately explaining the real basis upon which this metaphorical language rests’.<sup>137</sup> The use of metaphorical language has also been decried on the basis that it would make the approach to piercing the veil difficult to apply as it avoids formulating a substantive principle and is

<sup>127</sup> *Supra* note 1 para 34.

<sup>128</sup> *Supra* note 44.

<sup>129</sup> *Idem* para 124.

<sup>130</sup> *Supra* note 62.

<sup>131</sup> *Idem* para 78.

<sup>132</sup> NY 84 (1926).

<sup>133</sup> At 94.

<sup>134</sup> *Ibid.*

<sup>135</sup> Thompson *op cit* note 114 at 624.

<sup>136</sup> *Supra* note 76.

<sup>137</sup> *Idem* at 757.

not particularly helpful in trying to identify broader principles for determining when the separate legal personality of a company may be ignored.<sup>138</sup>

It is submitted that, perhaps by South African courts taking heed of these criticisms of the use of metaphors and descriptive terms such as ‘sham’, ‘device’, ‘stratagem’, ‘mask’, ‘cloak’, ‘alter ego’ and so forth, and avoiding the use of such metaphors and pejorative expressions, this would contribute towards the eradication of some of the confusion and uncertainty surrounding the doctrine of piercing the corporate veil in South African law. It would also contribute towards the proper development and interpretation of section 20(9) of the Companies Act in a manner that is clear and unambiguous, and with reasons for the conclusions reached being clearly and rationally explained.

*(b) Avoiding morality triumphing over legal principle*

*Gore’s* case also referred to the balancing of the need to give effect to the concept of separate legal personality, on the one hand, as against the adverse ‘moral’<sup>139</sup> and economic effects of countenancing an unconscionable abuse of the concept by the controllers of the company, on the other. The court thus regarded the adverse moral effects of the unconscionable abuse as a factor to be taken into consideration in the balancing approach. One could perhaps argue that the word ‘unconscionable’ implies some form of moral consideration, but the question arises whether morality should indeed be taken into consideration in the balancing approach.

The question before the court in *Antonio Gramsci Shipping Corp v Stepanovs*<sup>140</sup> was the very same question that was before the court in *VTB Capital plc v Nutritek International Corp*:<sup>141</sup> that is, whether the corporate veil could be pierced to hold non-contracting parties contractually bound under an agreement entered into by a separate entity that was controlled by them. The High Court in *Antonio Gramsci Shipping Corp v Stepanovs* found that the corporate veil could be pierced to allow contractual claims to be brought against non-contracting parties, and concluded that in situations where the contracting party was merely a ‘puppet’ company, a victim may bring a contractual claim against both the ‘puppet’ company and the non-contracting ‘puppeteer’, who ‘all the

<sup>138</sup> See Thompson op cit note 114 at 624; David Kershaw *Company Law in Context: Text and Materials* 2 ed (2012) 57 and Gevurtz op cit note 117 at 70.

<sup>139</sup> Supra note 1 para 29.

<sup>140</sup> *Antonio Gramsci Shipping Corp v Stepanovs* [2012] BCC 182.

<sup>141</sup> Supra note 44.

time, was pulling the strings'.<sup>142</sup> However the Supreme Court in *VTB Capital plc v Nutritek International Corp* overruled *Antonio Gramsci Shipping Corp v Stepanovs* and held instead that there was an overwhelming case against extending the principle of piercing the corporate veil in this way.<sup>143</sup> Lord Neuberger proclaimed that a strong justification is required before a court would be prepared to extend the principle of piercing the corporate veil in this manner,<sup>144</sup> and ruled that the conclusion of *Antonio Gramsci Shipping Corp v Stepanovs* was

‘driven by an understandable desire to ensure that an individual who appears to have been the moving spirit behind a dishonourable (or worse) transaction, action, or receipt, should not be able to avoid liability by relying on the fact that the transaction, action, or receipt was effected through the medium . . . of a company’.<sup>145</sup>

The Supreme Court found this to be an insufficient reason for justifying piercing the corporate veil in order to render that individual a party to the contract.<sup>146</sup> The rejection of morality as a factor in piercing the corporate veil is reinforced by the United Kingdom Supreme Court in its rejection of the use of metaphors and pejorative expressions in the context of piercing the veil, as previously discussed, on the ground that such expressions enable moral indignation to triumph over legal principle.

It is submitted that, having regard to the rejection of morality as a factor in determining whether to pierce the corporate veil by the United Kingdom Supreme Court and, particularly in the light of section 5(2) of the Companies Act in South Africa, which provides that, to the extent appropriate, courts may consider foreign law in interpreting or applying the Companies Act, in the event of courts considering the moral effects of countenancing an unconscionable abuse of the legal personality of the company in the balancing approach, as held by *Gore*, they must exercise caution to ensure that moral indignation does not in fact triumph over legal principle. If moral indignation were to do so, this would cloud the legal principles in issue and would cause confusion and uncertainty

<sup>142</sup> Supra note 140 para 26.

<sup>143</sup> Supra note 44 paras 137 and 147. The Supreme Court held that this proposed extension to the principle of piercing the corporate veil was all the more difficult to justify, given that the appellant could seek damages on the basis of negligent or fraudulent misrepresentation (para 139).

<sup>144</sup> Supra note 44 para 137.

<sup>145</sup> Idem para 147.

<sup>146</sup> Ibid.

in the legal principles applicable to piercing the corporate veil under section 20(9) of the Companies Act.

## V CONCLUSION

Section 20(9) of the Companies Act has conferred extensive powers on the South African courts to pierce the corporate veil, powers that do not exist under common law. The provision represents a new direction and shift in thinking in regard to the remedy of piercing the corporate veil. Some elements of section 20(9) of the Companies Act which illustrate the width of the provision and the wide powers given to courts are as follows:

- (i) Section 20(9) may be invoked by a court of its own initiative, regardless of whether the litigant in the matter before the court has requested the court to do so.
- (ii) Courts have been given the very widest of powers to grant consequential relief under section 20(9) of the Companies Act.
- (iii) The words 'interested person' have been given a wide meaning by *Gore*, which is arguably wider than the meaning given to the similarly worded section 65 of the Close Corporations Act, where a financial or monetary interest is an essential prerequisite. It is questionable whether this was the intention of *Gore* and whether it correctly reflects the legal position.
- (iv) The words 'unconscionable abuse' in section 20(9) have been given a very wide meaning by *Gore*. A much lower level of abuse is required under section 20(9) of the Companies Act as compared to that under section 65 of the Close Corporations Act before the corporate veil may be pierced. It may be that too low a level or threshold of abuse has been set by *Gore*.
- (v) An application under section 20(9) may be brought whenever the illegitimate use of the company's separate legal personality affects one in a way that should not reasonably be countenanced.
- (vi) The wide meaning given to the term 'unconscionable abuse', together with the liberal approach adopted by *Gore* in regard to the application of section 20(9), make it clear that the legal bases upon which courts have been prepared to pierce the corporate veil under the common law have been considerably extended under section 20(9) of the Companies Act.
- (vii) Section 20(9) is not a remedy of last resort and is not to be regarded as an exceptional remedy, as is arguably the case under the common law.

The common-law doctrine of piercing the corporate veil has not been repealed by section 20(9) of the Companies Act. It is submitted that the

common-law principles of piercing the corporate veil continue to serve as useful guidelines in interpreting section 20(9) of the Companies Act. It is submitted further that the balancing approach, stated in *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd*<sup>147</sup> and endorsed by *Gore*,<sup>148</sup> which requires a court to balance the need to preserve a company's separate legal personality against policy considerations which arise in favour of piercing the corporate veil, must be carefully applied by the courts in exercising their discretion whether to pierce the corporate veil under section 20(9) of the Companies Act. This approach may ensure that, in the light of the wide powers given to the courts to pierce the corporate veil under section 20(9) of the Companies Act, courts do not disregard the corporate veil too lightly, or risk making unfounded inroads into the overarching principles of separate legal personality laid down in section 19(1) of the Companies Act, *Salomon v Salomon*<sup>149</sup> and *Dadoo Ltd v Krugersdorp Municipal Council*.<sup>150</sup> It is essential that courts exercise their discretion to pierce the corporate veil wisely and that they exercise caution to ensure that they do not develop in the South African law a disproportionate and inappropriate application of the doctrine of piercing the corporate veil, as has occurred in Brazil, which also has a statutory remedy of piercing the corporate veil.

It is submitted further that in the light of the uncertainty and confusion which exists in regard to the doctrine of piercing the corporate veil in the South African common law as well as that of several leading foreign jurisdictions, courts must strive to interpret and apply section 20(9) of the Companies Act in a way that will maintain clarity and simplicity, so as to demystify the confusion surrounding the doctrine at common law. It is submitted that one way of doing this would be for courts to refrain from using metaphors and pejorative expressions in their judgments as such expressions may obstruct substantive principles being formulated, and may thereby cause confusion and uncertainty. It is submitted in addition that in applying section 20(9) of the Companies Act, courts must exercise caution to ensure that moral indignation does not triumph over legal principle, as this could cloud the legal principles in issue and cause more confusion and uncertainty.

Even though some of the questions and uncertainties regarding the interpretation of section 20(9) of the Companies Act have been

<sup>147</sup> Supra note 6 at 803.

<sup>148</sup> Supra note 1 para 29.

<sup>149</sup> Supra note 82.

<sup>150</sup> Supra note 86.

addressed in *Gore*, what remains unclear is the effect of the liberal powers given to courts by section 20(9) of the Companies Act and by *Gore* to pierce the corporate veil of companies. This remains to be seen.

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