

SOUTH AFRICA / JUDGMENT

Swarts and Others v Hart and Others (EL791/2018) [2019] ZAECELLC 19 (3 September 2019)

[2019] ZAECELLC 19

COURT

Eastern Cape High Court, East London Local Court

BEFORE

J.E Smith

CASE / FILE NUMBER

EL791/2018

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IN

THE HIGH COURT OF SOUTH AFRICA
(EAST
LONDON CIRCUIT LOCAL DIVISION)
CASE NO.: EL 791/2018

In

the matter between:

MARINDA
MARI SWARTS
First
Applicant
COLIN
DAVID McALL
Second Applicant
ANDREW
DAVID PRITCHARD
Third Applicant
JACOBUS
JOHANNES LOMBARD
Fourth
Applicant
And
ANDREW
NEIL HART First
Respondent
BRINKMAN
NDAYI McALL CC
Second Respondent

THE
REGISTRAR OF COMPANIES AND
CLOSE
CORPORATIONS Third
Respondent

JUDGMENT

SMITH J:

- [1] The applicants seek an order in terms of section 36 of the Close Corporations Act, No. 69 of 1984 (“the Act”) that the first respondent (“Hart”) shall cease, from the date of the order, to be a member of the second respondent. The latter is a multi-disciplinary practice rendering architectural, quantity surveying, and project management services in the construction industry. Section 36(1) of the Act provides, inter alia, for cessation of membership if: a member is guilty of conduct likely to have a prejudicial effect on the operations of the business; a member conducts him or herself, in relation to the corporation’s business, in such a manner that it is not reasonably practical for other members to carry on the business; or circumstances have arisen which render it just and equitable that the member should cease to be a member of the corporation. If any of the aforementioned factors are established, the court may order the transfer of the member’s interest, and determine an amount in respect of that interest.
- [2] The first applicant is an architect and member of the second respondent. The second applicant is a quantity surveyor, and the third and fourth applicants are also architects. All of them are employed by the second respondent.
- [3] The first respondent (Hart) is an architect and member of the second respondent. He is based at the second respondent’s East London office. Between them the first applicant and Hart own the entire members’ interest in the second respondent.
- [4] As mentioned above, the second respondent is a multi-disciplinary practice which is mainly engaged in the public sector where it renders services to various provincial and national organs of state.
- [5] The third respondent, namely the Registrar of Companies and Close Corporations, has been cited as an interested party only, and no substantive relief is sought against him.
- [6] The relief sought by the first applicant is for: the cessation of Hart’s membership in the second respondent; his membership interest to be acquired by her; the percentage of interest to be transferred to be determined in case number 1248/2017; and the amount to be paid to Hart to be determined by one David Robertson, a Chartered Accountant.

- [7] Subsequently, and apparently in response to the Hart's assertion that it is the Court that must determine the amount in respect of a member's interest, the applicants applied to amend their notice of motion to the effect that the value of Hart's member's interest must be determined by the Court, after hearing oral evidence, alternatively, by an independent accountant appointed by the South African Institute of Chartered Accountants, instead of by Robertson as originally prayed for.
- [8] After launching these proceedings, the applicants instituted application proceedings under case number 1248/2017 in which they sought an order declaring their respective membership interests in the second respondent to be as follows: first applicant 22.49%; the second, third and fourth applicants each 18.34%; and Hart 22.49%. That application has since been finalised, and in a judgment delivered on 29 March 2019, Griffiths J found that the applicants' assertion in respect of the nominee holding of interest on behalf of second, third and fourth applicants, had no factual foundation.
- [9] In that application, as is the case in the present proceedings, the first applicant contended that first applicant and Hart held a portion of their respective member's interest on behalf of the other applicants. A substantial portion of the applicants' founding papers in these proceedings has been dedicated to establishing that Hart's "disingenuous insistence" that he holds 50% of the member's interests in the second respondent, and his "malicious refusal" to acknowledge the agreement relating to the nominee holding on behalf of the other applicants, have a prejudicial effect on the operations of the practise.
- [10] While this contention is but one of the grounds which the applicants proffer in support of their assertion that they are entitled to invoke the provisions of section 36 of the Act, there can be little doubt, even on a perfunctory reading of the founding papers, that the dispute regarding the alleged nominee holding has been put up as the root cause of the contended breakdown in their relationship.
- [11] Mr Beyleveld SC, who appeared for the applicants, conceded that Griffiths J's judgment is dispositive of that issue. I accordingly do not have to concern myself with the substantial allegations relating to nominee holdings.
- [12] In addition, the applicants also aver that the second respondent's East London branch, which is managed by Hart, is being run at a loss. They contend that Hart is obstinately refusing to acknowledge this problem. He has also failed to follow company protocol regarding the appointment of staff and salary increases, which he has implemented without consultation.
- [13] They also aver that he has taken a disproportionate number of projects on risk, thereby causing the practice to suffer financial losses. In addition, despite having been advised by the Department of Roads and Public Works not to tender in a particular project because the second respondent's Mthatha office (being the closest to the project), would submit a bid, he nevertheless submitted a tender bid at an unreasonable discount.

- [14] They further allege that there has also been a complaint from a government department relating to poor performance which Hart has failed to address adequately. He also concluded a lease agreement with the second respondent in respect of premises owned by him, despite the fact that those premises had not been properly zoned for business use.
- [15] And, in a rather anecdotal manner, they point to an intercepted email which confirmed a payment to Hart's wife as being proof of the fact that he is conducting a "parallel" business from the East London office.
- [16] They contend that the relationship between them and Hart has consequently irretrievably broken down, hence the need for the cessation of his membership.
- [17] In his answering affidavit Hart denies any agreement relating to nominee ownership, and asserts his entitlement to insist on strict compliance with the terms of the Association and Operational Agreements.
- [18] In the light of the fact that the issue of the nominee holding is no longer extant, it is perhaps helpful at this stage to consider the terms of the Operational Agreement which was concluded in order to "create and record the terms of an Operational Committee to facilitate the management of the Corporation's business and as a framework for the structuring of remuneration of the Executives".
- [19] The following then are the salient features of that agreement: (a) the agreement records and regulates the employment and remuneration of executive employees; (b) it provides for their retirement and circumstances under which their employment may be terminated;
- (c) it provides for the establishment of management and executive committees, respectively ;
- (d) it records the conditions under which executives lend money to the business; (
- e) and contain provisions relating to the resolution of disputes, in particular providing that disputes arising out of and pursuant to the agreement "shall be submitted to informal arbitration"
- on the basis provided in the agreement.
- [20] The Association Agreement regulates the usual matters, such as the respective members' interests; employment; management; sureties; and loan accounts.
- [21] For the reasons which I have set out above, it is also not necessary for me to consider and pronounce upon the validity of Hart's comprehensive answers to the allegations pertaining to nominee shareholding. His responses to the remaining grounds relied upon by the applicants have been equally comprehensive and compelling. They can be summarised as follows: (a) regarding the allegations relating to the profitability of the East London office, he challenges the first applicant's bona fides, accusing her of deliberately excluding certain financial information and distorting the facts to support her "fallacious assertions"

regarding the profitability of that office; (b) he avers that the first applicant contrived to hamper the productivity of the East

London office by deliberately withholding payments for rental and electricity, poaching clients, and causing friction by paying

selective bonuses to other employees; (c) he asserts that it is standard practice to undertake work on risk, since employees who are not gainfully employed elsewhere can be employed on a commission basis to do the work; (d) he states that the complaint from the department was based on a misunderstanding, and the relevant functionary had apologised after he had been apprised of the true

facts; (e) in the respect of the premises leased by the practice, he states that it had been properly rezoned for professional use; and

(f) regarding the payment to his wife he states that it had nothing to do with architectural services but had rather been in respect of a proposal relating to a proposed leasing scheme that she had prepared on behalf of one of the second respondent's business associates, one Sotyato. That amount was subsequently paid to Sotyato. The reference to J.M Hart Architects was an obvious error since the transaction had nothing to do with the practice.

[22] The applicants bear the onus of establishing the grounds mentioned in section 36 (1) of the Act. In *Geaney vs Portion 117 Kalkheuwel Properties CC and others* 1998 (1) SA 622 (TPD), Kirk-Cohen J held, at 631H, that :

"A member of a close corporation seeking to invoke the provisions of section 36(1)

(d) quite obviously bears the onus to prove the relief he seeks. He must set out the relevant facts to place the Court in a position:

(1) to decide whether on the facts it can and should grant an order in terms of ss 1(a), (b), (c), and (d);

(2) to carry out its functions in terms of ss (2) and, in particular, to decide what financial adjustments to make."

[23] In the course of his argument Mr Beyleveld accepted that Griffith J's pronouncement on the nominee shareholding issue meant that the relief sought in terms of paragraph

1.2 of the notice of motion (namely the determination of the percentage of member's interest) was no longer sustainable. It is for this reason that the amended notice of motion sought to delete that paragraph. Mr Beyleveld's argument accordingly proceeded on the basis that the residual position should be adopted, namely that Hart holds 50% of the members' interest.

- [24] He nevertheless submitted that apart from Hart's refusal to acknowledge that he holds a percentage of his member's interest as nominee, there are other disputes which have arisen between the parties and which have escalated to an extent where there is virtually no meaningful communication between them.
- [25] He submitted further that, in addition, even though Hart denies that the trust relationship between the parties has broken down; he himself complains that he is being treated unfairly by the applicants in numerous respects. The totality of the evidence, however, points to the fact that the relationship between the members has in fact broken down irretrievably, and their inability to communicate meaningfully is prejudicially impacting on the effective running of the business. It is thus imperative that Hart ceases to be a member of the second respondent on any one or more of the grounds mentioned in sections 36 of the Act, or so the argument went.
- [26] Mr Beyleveld has also applied that in the alternative, in the event that the Court finds that the matter cannot be resolved on the papers, it should be referred for the hearing of oral evidence.
- [27] Mr Paterson SC, who acted for Hart, submitted that even though the judgment in case no. 1248/2017 has disposed of the issue relating to the nominee shareholding, the assertion that Hart has refused to acknowledge the nominee holding of his member's interest is inextricably linked to, and taints all the other allegations. He argued that all those complaints have their roots in that allegation.
- [28] This submission, in my view, has great merit. On a reasonable reading of the founding papers one gains the impression that Hart's refusal to acknowledge the nominee holding was the main thrust of the application and the main ground for the invocation of section 36.
36. All the other problems, which appear to have been brought about by a lack of communication, had their roots in that dispute, and had undoubtedly been proffered merely as adjuncts to that main complaint.
- [29] Mr Paterson has correctly submitted that Griffiths J's judgment has far-reaching consequences for this application. First, it means that

Hart's insistence upon the strict observance of the terms of the Association and Operational Agreements, was justified. And

second, the remaining conflicts appear mainly to relate to disagreements regarding the management of the business. The question

then arises as to whether the grounds mentioned in section 36 of the Act have been established on a balance of probabilities.

- [30] It is trite that if the matter is decided on the papers, then it must be resolved on Hart's version. As I have mentioned earlier, his answers to the applicants' allegations are comprehensive and plausible. I am accordingly satisfied that they are not so far-fetched and uncreditworthy that they can be rejected out of hand.
- [31] If the matter is approached on this basis, then it is clear that the disputes between the parties (if one ignores the issue relating to nominee shareholding) relate to management issues that can, and should, be resolved through normal business conventions, or the terms of the Association and Operational Agreements.
- [32] In order for the Court to grant relief in terms of section 36 (1) (b) of the Act, it must be satisfied that the member is guilty of conduct that "taking into account the nature of the corporation's business", is likely to have a prejudicial effect on the carrying on of the business.
- [33] And as I have mentioned previously, the onus is on the applicants to establish this ground on a balance of probabilities. The "guilt" which the applicants have sought to impute to Hart related to his alleged "obstinate and disingenuous" refusal to acknowledge the nominee shareholding agreement. There can be little doubt that had the applicants been able to establish that allegation in the matter before Griffiths J, Hart's "guilt" would in all probability have been established. Conversely, the fact that Griffiths J found the allegations to have been without a factual basis, means that the applicants have failed to establish the requirement of that subsection on a balance of probabilities.
- [34] Reliance on subsection 36 (1) (c) requires of the applicants to establish conduct by Hart "in matters relating to the corporations business" that makes it not reasonably practical for the other members to carry on the business of the corporation with him. Mr Paterson has in this regard also correctly submitted that Griffiths J's judgment means that Hart's insistence on the observance of the terms of the Association and Operational Agreements was reasonable. The applicants have accordingly also failed to establish this jurisdictional fact on a balance of probabilities.
- [35] The ground mentioned in subsection 36 (1) (d), namely "that circumstances have arisen, which render it just and equitable that such member should cease to be a member of the corporation", can also not survive the impact of Griffith J's pronouncement on the nominee holding issue. It can, by no stretch of the imagination, be contended that a member who has justifiably insisted on the implementation and observance an Association Agreement, can be justly and equitably removed as a member.
- [36] Mr Beyleveld also subsequently referred me to the Supreme Court of Appeal judgment in *Freedom Stationery (Pty) Ltd and Others v Hassan and Others* 2019 (4) SA 459 (SCA) which concerned the interpretation of section 252 of the Companies Act, 61 of 1973. That section was subsequently repealed by the new Companies Act, no, 71 of 2008, but was substantially re-enacted in section 163 of the new Act. Van der Merwe JA held that once it had been established that there has been "oppressive or unfairly prejudicial conduct" within the

meaning of ss. 252 (1) or (3) of the Act, the Court has wide powers to make an order that it considers just and equitable in the circumstances. The Court may, for example compel a minority shareholder to purchase the shares of a majority shareholder, or grant relief against “an oppressor” who is not a shareholder of the company. And the powers of the Court

are not restricted to orders relating to the pursuance of the objects contained in a company’s memorandum of incorporation. This decision was obviously proffered in support of Mr Beyleveld’s submission that the Court has wide powers to grant relief under section 36 (1) (d), if the facts establish that it would be just and equitable that a member should cease to be member of a corporation. The facts of Freedom Stationary are, however, distinguishable. As I have mentioned above, without the allegations relating to the nominee shareholding, the remaining disputes are not of such a nature that they cannot be resolved in terms of existing agreements. Furthermore, those allegations relate essentially to Hart’s insistence on the strict compliance with those agreements. In these circumstances it would indeed be unjust and inequitable for the Court to order the cessation of his membership.

- [37] In the light of my finding that none of the grounds mentioned in section 36 has been established, it is not necessary for me to deal with the arguments relating to the appropriate mechanism for the valuation of Hart’s member’s interest.
- [38] I also do not believe that there are any prospects that the hearing of oral evidence will disturb the probabilities. As I have mentioned earlier, without the nominee holding issue, the remaining disputes relate to the management of the practice, and must be addressed in terms of the Association and Operational Agreements. This is the case regardless of which version is accepted. The application for referral for oral evidence must accordingly also fail.
- [39] Regarding the matter of costs, there remains the issue as to which party ought to be held responsible for the costs of a previous appearance on 13 June 2019, when the matter could not proceed through no fault of any of the parties. What had apparently happened was that as a result of a misunderstanding, the matter, despite having been properly set down for hearing (and both counsel having been ready to argue), the parties were informed that the matter had only been set down provisionally, and that there was not a judge available to hear the matter. In my view none of the parties can be blamed for the costs occasioned by that postponement. I think that it is only appropriate and fair, in such circumstances, that each party should bear his or her own costs.
- [40] In the result the application is dismissed, with costs, excluding the costs occasioned by the postponement on 13 June 2019.

J.E SMITH

JUDGE OF THE HIGH COURT

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