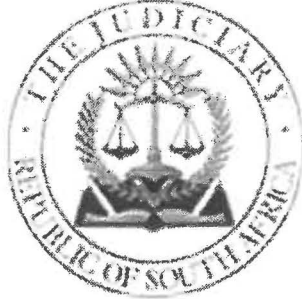


REPUBLIC OF SOUTH AFRICA



IN THE HIGH COURT OF SOUTH AFRICA
GAUTENG DIVISION, JOHANNESBURG

CASE NO: 15511/2018

[1]	REPORTABLE. YES/ <u>NO</u>
[2]	OF INTEREST TO OTHER JUDGES. YES/ <u>NO</u>
[3]	REVISED.
<u>20/5/19</u>	
Date:	<u>WHG VAN DER LINDE</u>

In the matter between:

Barloworld Logistics Africa (Pty) Ltd

1st Plaintiff/Respondent

Barloworld Transport (Pty) Ltd

2nd Plaintiff/Respondent

and

Steven Michael Ford

1st Defendant/Excipient

Robert Arthur Lumn

2nd Defendant/Excipient

Amanda Cynthia Fairley

3rd Defendant/Excipient

Iain Robertson Douglas

4th Defendant

Dylan Arthur Barrie McNamara

5th Defendant

Enigma Transport Logistics (Pty) Ltd

6th Defendant

Giratime (Pty) Ltd

7th Defendant

Nyladox (Pty) Ltd

8th Defendant

JUDGMENT

Summary:

Exception against particulars of claim on the basis of vague and embarrassing. Plaintiffs pleading fraud consisting of defendants knowingly participating in accounting treatment failing to conform to "generally accepted accounting practice";

Plaintiffs failing to particularise particular standard of practice said to comprise "generally accepted accounting practice";

Held: SA GAAP no longer being issued by Accounting Practices Board, which no longer exists;

Held further: even if informal non-promulgated standards of International Financial Reporting Standards (IFRS) have developed, and even if these may be referred to as "gaap", insufficiently particularised to enable defendants properly to plead to cause of action.

Exception upheld.

Van der Linde, J:

Introduction and background:

- [1] The first three defendants except to the plaintiffs' particulars of claim as being vague and embarrassing. In the summons the plaintiffs claim money judgments against the eight defendants. The plaintiffs also claim against the 1st defendant rectification of what is called "*the separation agreement*", and as against the 1st and 2nd defendants, declaring each of them to be delinquent; and, in the alternative, ordering that the two of them be declared and placed under probation for a period of five years.
- [2] The claims are formulated in four separate claims, the first being against the 1st, 2nd and 3rd defendants jointly and severally, with alternative claims against each of the first three defendants separately. The second claim is against the 4th, 5th, 6th, 7th and 8th defendants jointly and severally, the third claim against only the 1st defendant, and the fourth claim only against the 1st and 2nd defendants.

- [3] The 6th, 7th and 8th defendants are companies and it is alleged that the 4th and 5th defendants were at all times directors of those three companies. The case starts with the assertion that a written employment agreement was entered into on 26 May 2011 between Barloworld Logistics (Pty) Ltd (not one of the plaintiffs) and the 1st defendant in terms of which the 1st defendant was employed as Chief Executive Officer for that company.
- [4] The particulars of claim then assert that earlier, by some three years, in September 2008, the same Barloworld company concluded a written employment agreement with the 2nd defendant in terms of which the 2nd defendant was employed as Financial Director for that Barloworld company. The particulars of claim then assert that on 20 March 2015 the employment of the 1st and 2nd defendants was transferred from Barloworld Logistics (Pty) Ltd to the 1st plaintiff in terms of section 197 of the Labour Relations Act, 1995.
- [5] Then it is asserted that on 22 October 2015 the 1st plaintiff concluded a written employment agreement with the 3rd defendant in terms of which the 3rd defendant was employed by the 1st defendant as Executive: Operations.
- [6] The particulars of claim assert that the 1st three defendants occupied senior managerial positions within the Barloworld group of companies and owed fiduciary duties to the plaintiffs. It is further asserted that the 1st and 2nd defendants were at all times directors of the two plaintiffs and owed them fiduciary duties both under the common law and in terms of section 76 of the Companies Act 71 of 2008 ("the Act").
- [7] The particulars of claim then assert against the 1st, 2nd and 3rd defendants what is called "*the relevant representations*" and that these were, to the knowledge of the 1st three defendants, false. Particulars of the alleged falsehoods, which given the allegations may also be described as frauds, are then asserted in paragraphs 27, 28 and 29 of the particulars of claim, respectively in respect of the amounts of R16 million, R3,1 million and R5,3 million.

- [8] The case which then unfolds as one for pure economic loss resulting from fraud, proceeds to assert in paragraph 30 that the relevant representations were material and made with the intention of overstating the 1st plaintiff's operating profit for the 2016 financial year, and to induce the 1st plaintiff to pay inflated incentives to, amongst others, the 1st, 2nd and 3rd defendants.
- [9] Pursuant to the fraud, the 1st defendant paid the inflated incentives in the 2016 financial year totalling R4 525 221, which is alleged to be made up of the incentive paid to the 1st defendant in the amount of R186 726, to the 2nd defendant the amount of R199 809, to the 3rd defendant the amount of R124 019, and to executives, management and employees other than the 1st three defendants, the aggregate amount of R4 014 667. These assertions give rise to the various claims for repayment and alternative relief under section 77(2)(a) of the Act.
- [10] The claims against the 4th, 5th, 6th, 7th and 8th defendants are not relevant because the exception is not brought by them.
- [11] The first three defendants' exception focusses on the accounting treatment of the annual financial statements of the 1st plaintiff's 2016 financial year which recognized an operating profit of R16 million in respect of logistical services rendered by the 1st plaintiff to the 6th defendant; of R3,1 million attributable to a license agreement with Emirates; and of R5,3 million attributable to the capitalising of intangible assets, aggregating R24,4 million. The plaintiffs contend that the first three defendants knowingly participated in this accounting treatment which was - to the knowledge of the first three defendants - false and, importantly for present purposes, non-compliant with what is called in the pleading, *"generally accepted accounting practice."*

- [12] The exception is that these averments are vague and embarrassing on two grounds. The first ground relates to the assertions concerning the operating profit, the generally accepted accounting practice, and profit shares. Two reasons are advanced for the proposition that the particulars of claim are vague and embarrassing in that regard. The first is that the particulars of claim do not explain what "*operating profit*" means, or how this was required to be calculated.
- [13] It is alleged that according to the Oxford Dictionary of English, "*operating profit*" means "*a gross profit before deduction of expenses*", and that on that definition the profit shares would have formed part of the gross profit and would as a natural consequence have been included in the calculation of operating profit.
- [14] The second reason why it is alleged that these averments are vague and embarrassing is that the particulars of claim do not set out which principles of "*generally accepted accounting practice*" were offended by the inclusion of the profit shares in the calculation of operating profit.
- [15] The second ground of objection is that the averment that the first three defendants participated in the accounting treatment by recognising R3,1 million as operating profit for the 2016 financial year attributable to a license agreement with Emirates, and the recognition of R5,3 million attributable to the capitalising of intangible assets, are vague and embarrassing because no details are set out as to when, where, how or with whom they so participated, and no details are set out as to when, where and how they so acquiesced, and the context in which they did so. Given my conclusion in respect of the first ground of objection, it is unnecessary to deal with the second.

Generally accepted accounting practice, GAAP and *gaap*

[16] The day before the hearing I sent a note to counsel for the parties asking them to assist me by identifying *“the consequences following on the withdrawal of SA GAAP in respect of financial years commencing on or after 1 December 2012, the voluntary winding-up of the Accounting Practices Board, and the application instead of IFRS”*. I had in mind the joint announcement by the Accounting Practices Board (APB) and the Financial Reporting Statements Council (FRSC) regarding SA GAAP. In terms of that announcement the APB would be voluntary wound-up, and SA GAAP would be withdrawn and will cease to apply in respect of financial years commencing on or after 1 December 2012.¹

[17] Some background is necessary.² The APB was formed in 1973 to consider what should be regarded as generally accepted accounting practice, and in fact to issue statements of SA GAAP. In time, the APB, having issued statements of SA GAAP for some 30 years, decided to harmonise SA GAAP with International Financial Reporting Standards (*“IFRS”*).

[18] Up to this point in time and for a while thereafter, section 286 of the then Companies Act 61 of 1973 required of the directors of a company in respect of any financial year to cause to be made out in one of the official languages, annual financial statements, and to lay them before the annual general meeting. That section also prescribed the contents of the annual financial statements and then continued in subsection (3) as follows (my emphasis):

“286. DUTY TO MAKE OUT ANNUAL FINANCIAL STATEMENTS AND TO LAY THEM BEFORE ANNUAL GENERAL MEETING.

(1) ...

(2) ...

(3) The annual financial statements of a company shall, in conformity with generally accepted accounting practice, fairly present the state of affairs of the company

¹ Some statutes have not kept up with the changes; compare Registrar of Medical Schemes and Another v Genesis Medical Scheme 2016 (6) SA 472 (SCA).

² Compare Commissioner, South African Revenue Service v Volkswagen South Africa (Pty) Ltd, 2019 (2) SA 362 (SCA).

and its business as at the end of the financial year concerned and the profit or loss of the company for that financial year and shall for that purpose be in accordance with and include at least the matters prescribed by Schedule 4, insofar as they are applicable, and comply with any other requirements of this Act."

[19] It is to be noted that the words "*generally accepted accounting practice*" in subsection 286(3) appeared in lower case. Until the issuance by the APB of statements of SA GAAP, there was no set of written rules indicating precisely what "*generally accepted accounting practice*" as envisaged in the statutory prescription was. Some general principles had evolved in the course of time, and these were regarded as guiding members of the accountancy profession both in South Africa and in the United Kingdom.

[20] With the issuance of formal statements of SA GAAP there developed practices, as explained by Meskin in *Henochsberg on the Companies Act*, Volume 1, page 550, which were colloquially referred to as "*gaap*" and "*GAAP*". The latter referred to the accounting practices that were described and prescribed in the formal statements issued by the APB. The former, often referred to by practitioners and commentators as "*little gaap*", were those practices that were extensions of and additional to the formal statements, and that had become generally accepted due to their being followed generally.

[21] In this context the 2nd edition of *Generally Accepted Accounting Practice – A South African Viewpoint*, Everingham and Hopkins say:³ "*The existing statements represent promulgated GAAP, but there has also grown up a body of, as yet, unpromulgated GAAP.*"

[22] Meskin puts it this way (my emphasis):

"The existence of unpromulgated gaap as a reporting framework may, however, have resulted in the adoption of unsound accounting practices because a number of entities were

³ At p2.

applying such practices. That was of course not a desirable state of affairs since users are financial statements who rely on them require an assurance that financial statements do indeed fairly present the affairs of the entity. In order to provide such assurance, legal backing for the South African accounting statements has long been regarded as essential. The required legal recognition for accounting statements will now be achieved by the introduction of this section."

- [23] The author was referring to the new section 285A by means of the Corporate Laws Amendment Act 24 of 2006 (14 December 2007).

- [24] Reverting then to the joint announcement of the APB and the FRSC regarding SA GAAP: The APB since 2003 decided to harmonise SA GAAP with IFRS. Since then, the APB had issued IFRS statements as SA GAAP without amendment. However, the chairpersons of the APB and the FRSC had decided, in order to reduce the burden of issuing each IFRS standard as SA GAAP, formally to withdraw SA GAAP, and that was the rationale for the joint statement. After 1 December 2012 the FRSC would acquire, by regulation, the power to issue financial reporting pronouncements to take account of local circumstances.

- [25] The effect of the joint announcement was that some companies were required to start preparing for their conversion from SA GAAP to IFRS, or depending on their size, to IFRS for small and medium enterprises. Further, with effect from May 2011, the APB ceased approving individual IFRS statements as SA GAAP.

- [26] And reverting then to "*little gaap*", Meskin draws attention to the judgment of Colman, J who observed in *Novick v Comair Holdings Ltd* 1979 (2) SA 116 (W) (my emphasis):

"The requirement that the fair presentation enjoined be in conformity with 'generally accepted accounting practice' is, in one sense, a limiting requirement. But it carries with it a measure of flexibility because there can be differences of opinion about what generally accepted accounting practice is in relation to certain matters; and there can be differences of professional opinion as to the application of accepted practices to specific situations."

[27] I revert to the request that I directed at counsel the day before the hearing: It seemed to me that if “*little gaap*” developed as an adjunct to SA GAAP, and since SA GAAP had disappeared with effect from 1 December 2012, there could well be a legitimate debate as to whether “*little gaap*” existed beyond that date. On the other hand, it might be said that in the practice of accounting, members of that profession may have continued developing “*little gaap*”; or they may instead have developed “*little ifrs*”.

[28] Either way, it seemed to me necessary to know what the position of the parties was on this score, given the centrality which “*generally accepted accounting practice*” assumes in the plaintiffs’ particulars of claim. I am grateful for the written note provided by the respondents/plaintiffs in response to my request.

Discussion

[29] That then brings me to a discussion of the merits of the exception. It will be recalled that the exception is not that no cause of action is disclosed, but instead that the particulars of claim are vague and embarrassing. Mr Brett SC who led Mr Kaplan for the excipients, took the court through the particulars of claim but particularly stressed the role in which *little gaap* is inspanned in the plaintiffs’ cause of fraudulent misrepresentation.

[30] The fraudulent misrepresentation pleaded follows the following logic: The 1st three defendants, by dint of the common law and the position of the 1st and 2nd defendants as directors, and the 3rd defendant by dint of being Executive: Operations, all owed fiduciary duties to the plaintiff; and they were in addition each responsible for the accurate and honest financial reporting in respect of both plaintiffs. As regards the 1st plaintiff, this applied to its financial records, including accounting entries and particularly the 1st plaintiff’s operating profit, which operating profit would be used to calculate the incentives payable to the executives.

- [31] The plaintiffs allege that the 1st three defendants, duty-bound in this way, knowingly participated in a particular accounting treatment in the accounting records of the plaintiffs, of the recognition of an amount of R16 million in respect of operating profit, an amount of R3,1 million in respect of operating profit, and an amount of R5,3 million as operating profit, totalling R24,4 million.
- [32] The particulars of claim then proceed to assert that to the knowledge of the 1st, 2nd and 3rd defendants this particular accounting treatment was false, “... *and the relevant accounting treatment did not comply with generally accepted accounting practice*”. It is further asserted that the 1st, 2nd and 3rd defendants deliberately represented to the plaintiffs that the particular accounting treatment did comply with generally accepted accounting practice.
- [33] In paragraph 27 and following the particulars of claim purport to explain why it was being asserted that the relevant accounting treatment did not comply with generally accepted accounting practice, by listing four reasons of asserted non-compliance; but, importantly, without identifying the particular feature or principle of generally accepted accounting practice that was not being complied with.
- [34] Mr Brett accordingly argued that absent the particular feature or principle of gaap, the particulars of claim were vague and embarrassing, because the defendant was unable to work out whether at all it had not complied with generally accepted accounting practice. He submitted in particular, as is specified in paragraph 3.1.3 of the notice to remove cause of complaint, that the particulars of claim did not set out what operating profit meant and how this was required to be calculated.
- [35] In short, the argument was that there was a disconnect apparent from the particulars of claim between the three essentials of the plaintiffs’ claim: what operating profit was required to comprise; how the 1st, 2nd and 3rd defendants’ treatment of operating profit

failed to comply with generally accepted accounting practice; and how this related to the asserted incentive bonuses.

[36] Mr Gilbert, who appeared with Mr Van Kerckhoven for the respondents/plaintiffs, argued however that the pleading, properly construed, used the words "*generally accepted accounting practice*" not as a term of art, but in the sense of requiring of the 1st, 2nd and 3rd defendants simply to act honestly and accurately in relation to the accounting statements.

[37] I do not believe that that is a fair reading of the pleading. The words "*accurately and honestly*" do appear, as one sees in subparagraphs 23.1, 23.2 and 23.3. But when the notion of "*generally accepted accounting practice*" is introduced in paragraph 25, this is in conjunction with and not as subsuming the requirement of accurate rendition of the accounting records.

[38] Further, having regard to the background of the notion of "*generally accepted accounting practice*" in the Companies Act 61 of 1973, one can hardly blame a defendant who reads the particulars of claim as referring to generally accepted accounting practice in the way in which this concept was understood in company law terms, as the many cases thrown up by an electronic word search will show.

[39] As I have indicated, to my mind, absent the identification of the particular accounting practice which was being offended by the accounting treatment asserted in paragraph 24 of the particulars of claim, the particulars of claim are rendered vague and embarrassing. And, as I have indicated, this relates not simply to one paragraph of the particulars of claim; bear in mind the lack of particularity of the concept of "*operating profit*" as well as the lack of particularity of the concept of "*incentive bonus*", and it seems to me that one is left with vagueness and embarrassment which goes to the whole cause of action, as envisaged in *Jowell v Bramwell-Jones and Others* 1998 (1) SA 836 (W).

[40] *Trope v South African Reserve Bank* 1992 (3) SA 208 (T) is authority for the proposition that an exception that a pleading is vague and embarrassing involves a twofold consideration: First, whether the pleading lacks particularity to the extent that it is vague; and the second being whether the vagueness causes embarrassment to such an extent that the excipient is prejudiced.

[41] In my view the pleading here fails on both scores. I have dealt with the vague and embarrassing aspect. The excipient is prejudiced because although it would be able to fashion a plea in the form of a meaningless denial, it will not have been able to address the material merits of the fraud cause of action which the plaintiffs are pressing against the 1st three defendants.

[42] In these circumstances in my view the exception is good, and I make the following order:

- (a) The 1st, 2nd and 3rd defendants' exception against the plaintiffs' particulars of claim is upheld;
- (b) The plaintiffs' particulars of claim are set aside;
- (c) The plaintiffs are afforded 20 days within which to amend their particulars of claim;
- (d) The plaintiffs are directed to pay the costs of the exception, including the costs occasioned by the employment of two counsel, one of whom is senior counsel.



WHG van der Linde
Judge, High Court
Johannesburg

Date argued: 15 May 2019

Date judgment: 21 May 2019

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