REPUBLIC OF SOUTH AFRICA

IN THE HIGH COURT OF SOUTH AFRICA

(LIMPOPO DIVISION, POLOKWANE)

(1)	REPORTABLE: YES/~~NO~~
(2)	OF INTEREST TO THE JUDGES: YES/~~NO~~
(3)	REVISED.
Signature	…………
Date……	23/01/2020

CASE NO: 7283/2018

In the matter between:

DION SVOBODA — **APPLICANT**

and

RONALD WALTER SPARROW — **FIRST RESPONDENT**

DRS THOHOYANDOU (PTY) LTD — **SECOND RESPONDENT**

THE COMPANIES AND INTELLECTUAL PROPERTY COMMISSION (CIPC) — **THIRD RESPONDENT**

JUDGMENT

MAKGOBA JP

[1] The Applicant brought an application to have the First Respondent declared a delinquent director in terms of the provisions of section 162(5)(c)(iv)(aa) & (bb) of the Companies Act No. 71 of 2008 and further that the First Respondent be removed as director of the Second respondent. The First Respondent opposed the application and launched a counter application for the liquidation of the Second Respondent in terms of section 81(1)(d) of the Companies Act, 2008 on the basis that it is just and equitable to do so as the Applicant and First Respondent are deadlocked.

[2] Each party prays for a costs order on attorney and client scale against the other party.

Common Cause Facts

[3] On the evidence before me the following facts are common cause or not in dispute:

3.1. The Applicant and the First Respondent are the only two directors of the Second Respondent Company ("the Company"). The Second Respondent renders security services in Thohoyandou, Giyani and Malamulele.

3.2. The Applicant has provided the lion's share of the start-up capital in respect of the Company and has a substantial loan account with the company in respect of which he is receiving a monthly repayment from the Company.

3.3. During July 2018 the Company and the Kremetart Residential Community in Giyani entered into an agreement in terms whereof a monthly fee would be paid to the Company for monitoring services. The Company also had to install alarm systems in 74 community members' houses. The Kremetart Residential Community deposited money due to the Company in terms of the said agreement into the First Respondent's personal bank account following a request to do so by the First Respondent.

No invoices were made out by the Company in respect of these payments. The clients were instead informed by the First Respondent via sms to furnish proof of payment to an Indian Spaza Shop.

3.4. The First Respondent has deliberately kept this information from the Applicant. The First Respondent has in this regard stated in his opposing affidavit that "I know if I were to tell him of the "plan" he would not have agreed to it" (The "him" referring to the Applicant).

3.5. The Applicant found out about this state of affairs. The First Respondent's said bank account was also used by him in his personal capacity. The First Respondent's monthly loan and credit card instalments were also deducted by way of debit order from the said bank account. This is the personal bank account of the First

Respondent into which the Company's clients were told to deposit monies due and payable to the Company.

3.6. Seventy four (74) alarm systems were in fact installed by the Second Respondent, that is the Company. However none of the profit was paid over to the Second Respondent Company.

3.7. In his defence the First Respondent stated that it was his intention that his personal bank account be used like "some sort of trust account" for the payment of deposits by the Company's clients and that it was his intention to pay any profit into the Company's bank account. The First Respondent stated furthermore that he intended to reimburse the clients for the erroneous payments of the monthly monitoring fees into his account.

3.8. It is common cause that profit and monthly monitoring fees were never paid over to the Company and its clients despite the First Respondent's aforesaid stated intentions.

Issues to be determined

[4] In the light of the factual background set out above the issue to be determined is whether the pre-requisites for an order declaring the First Respondent a delinquent director as requested by the Applicant have been met. In this regard the following unjustified conduct of the First Respondent should be noted:

4.1. Money due and payable by clients of the Second Respondent Company was at the request of the First Respondent paid into his personal bank account.

4.2. These clients were not invoiced by the Second Respondent Company instead they were requested by the First Respondent to submit proof of payment at an Indian Spaza Shop.

4.3. The First Respondent had deliberately hidden this fact from the Applicant.

4.4. The money paid into the First Respondent's account by the Second Respondent's clients commixed with the money in his account. Some of the money paid into the First Respondent's bank account was used by him for personal gain.

[5] In an effort to justify his conduct the First Respondent has these to say:

5.1. That the First Respondent never had any control of the Company's finances, which are run by the Applicant to the exclusion of the First Respondent. That the First Respondent was only doing ground work of the Company.

5.2. The First Respondent has on numerous occasions in the past approached the Applicant to buy inter alia vehicles, motorbikes and firearms for certain projects and to accommodate growth in the company but it fell on deaf ears.

5.3. The Company struggled to make ends meet and could not always pay its monthly commitments.

5.4. The Company could not provide equipment to clients who had already paid for it.

5.5. The Applicant unilaterally drew more and more monies from the Company contrary to the agreement between the parties which placed the Company under financial constraints.

5.6. That it was never the First Respondent's intention to take the monies for his personal gain and he did not do so, the only reason why he allowed the clients to pay their money into his personal bank account is because the Company was having serious cash flow problems and he made sure the Company would comply with its contractual obligations.

5.7. The First Respondent did not inform the Applicant of his plan because the Applicant was simply not approachable in this regard.

5.8. The First Respondent therefore denies any willful negligence or willful misconduct or a breach of his fiduciary duties towards the Company.

5.9. According to the First Respondent the trust relationship between him and the Applicant had broken down and that the two are at loggerheads with each other. The Applicant and the First Respondent will not be able to work together now or in the near future.

Legal Framework

[6] Section 162(5)(c) of the Companies Act 71 of 2008 read with sections 76(2),76(3) and 77(3) of the Act provides for the pre-requisites that have to be met for declaring a director of a Company a delinquent. What follows are the provisions of the appropriate sections of the Companies Act, 2008.

[7] Section 76(2)(a) of the Companies Act, 2008 deals with, inter alia, standards of conduct and liabilities of directors.

Section 76(2) reads as follows:

"(2) A director of a company must—

(a) not use the position of director, or any information obtained while acting in the capacity of a director—

(i) to gain an advantage for the director, or for another person other than the company or a wholly-owned subsidiary of the company; or

(ii) to knowingly cause harm to the company or a subsidiary of the company; and

(b) communicate to the board at the earliest practicable opportunity any information that comes to the director's attention, unless the director—

(i) reasonably believes that the information is—

(aa) immaterial to the company; or

(bb) generally available to the public, or known to the other directors; or

(ii) is bound not to disclose that information by a legal or ethical obligation of confidentiality.

(3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director—

(a) in good faith and for a proper purpose;

(b) in the best interests of the company; and

(c) with the degree of care, skill and diligence that may reasonably be expected of a person—

(i) carrying out the same functions in relation to the company as those carried out by that director; and

(ii) having the general knowledge, skill and experience of that director."

[9] *Section 77(3) reads:*

"(3) A director of a company is liable for any loss, damages or costs sustained by the company as a direct or indirect consequence of the director having—

(a) acted in the name of the company, signed anything on behalf of the company, or purported to bind the company or authorise the taking of

any action by or on behalf of the company, despite knowing that the director lacked the authority to do so;

(b) acquiesced in the carrying on of the company's business despite knowing that it was being conducted in a manner prohibited by section 22(1);

(c) been a party to an act or omission by the company despite knowing that the act or omission was calculated to defraud a creditor, employee or shareholder of the company, or had another fraudulent purpose"

[10] Section 162(5)(c) provides:

"(5) A court must make an order declaring a person to be a delinquent director if the person—

(c) while a director—

(i) grossly abused the position of director;

(ii) took personal advantage of information or an opportunity, contrary to section 76(2)(a);

(iii) intentionally, or by gross negligence, inflicted harm upon the company or a subsidiary of the company, contrary to section 76(2)(a);

(iv) acted in a manner—

(aa) that amounted to gross negligence, wilful misconduct or breach of trust in relation to the performance of the director's functions within, and duties to, the company; or

(bb) contemplated in section 77(3)(a), (b) or (c);".

Applicant's Submissions

[11] The Applicant submits that in the light of the undisputed and / or common facts outlined herein, a proper case for an order declaring the First Respondent a delinquent director has been made out and for the following reasons:

11.1. The First Respondent acted without authority when he proposed to the Kremetart Residential Community to deposit money destined for the Second Respondent Company into his personal bank account. The First Respondent furthermore acted as such knowingly that he lacked the authority to do so.

11.2. The First Respondent's conduct as such (allowing clients of the Second Respondent to pay money destined for the Second Respondent into his personal bank account) amounts to wilful misconduct on his part as well as a breach of trust as envisaged in Section 162(5)(c)(iv)(aa) and (bb) of the Act.

11.3. Having acted in the name of the Second Respondent Company despite knowing that he lacked necessary authority to do so furthermore constituted a clear breach of the provisions of Section 77(3)(a) of the Act.

11.4. The First Respondent utilised money destined for the Second Respondent for his own benefit. The conduct of the First Respondent in his dealings with the affairs of the Second Respondent did not measure up to standard required and expected of a director and was in breach of his fiduciary duties to the Second Respondent.

11.5. The First Respondent furthermore did not communicate this information to the Applicant. Section 76(2)(b) creates a duty on the part of a director to communicate at the earliest practicable opportunity any information that comes to his attention to his Board of Directors. The First Respondent stated that "the Applicant was simply not approachable in this regard".

11.6. Even if the relationship between the First Respondent and the Applicant was strained he was nevertheless bound by his legal duty as a director to discharge his duties in the same manner had the relationship between them been normal. Furthermore even if the Applicant also acted in dereliction of his duties to the Second Respondent as alleged by the First Respondent (which is denied by the Applicant) that did not absolve the First Respondent from failing to carry out his duties to the Second Respondent.

11.7. It has been unequivocally conceded by the First Respondent that he had acted behind the Applicant's back as the Applicant would have never agreed to clients paying money into the First Respondents personal bank account but nevertheless embarked on such in reckless disregard of his duties as director to the Second Respondent.

11.8. The First Respondent has been guilty of wilful misconduct and breach of trust in relation of the performance of his duties and functions as a director and acted in breach of Section 77(3)(a) in that he acted in the name of the Second Respondent despite knowing that he lacked the authority to do so. The First Respondent has also acted in breach of his fiduciary duties to the Second Respondent. A person in a fiduciary position is obliged in dealing with the money of the beneficiary to observe due care and diligence and not to expose it in any way to any business risks.

11.9. The Respondent has proven himself to be unable to manage the business of the Second Respondent or have fail in or is in neglect of his duties and obligations as a director of the Second Respondent.

[12] I agree with the above submissions made by the Applicant's Counsel that the First Respondent's conduct would justify for an order that she be declared a delinquent director.

The Law

[13] The effect of a declaration of a person as a delinquent director is that he is thereupon disqualified, for so long as the declaration remains in force, from being a director of any company. In the declaration of a person as a delinquent director what is required to be established is conduct intended to harm the company, alternatively an attitude of recklessness by the director in the face of an appreciation that this conduct could cause the company harm. The relevant causes of delinquency entail either dishonesty, wilful misconduct or gross negligence. The applicant in such proceedings must allege that the respondent conducted himself or herself with the intention of harming the company.

See **Lewis Group Ltd v Woolman and Others (1) [2017] 1 All SA 192 (WCC)**.

[14] The bar is set too high to justify an order of delinquency. In **Gihwala and Others v Grancy Property Ltd and Others [2016] 2 All SA 649 (SCA)** it was held that delinquency was justified where it is found that the directors have been guilty of gross abuses of their positions in circumstances where they owed a fiduciary duty to ensure that the company complied with terms of an investment agreement. This entails a breach of trust in relation to the performance of one's duty as a director.

In essence the Supreme Court of Appeal held in **Gihwala** that for an application to succed in terms of section 162(5)(c) of the Companies Act a delinquency order can only be made in consequences of serious misconduct on the part of a director,.

[15] Section 162(5) makes it peremptory for a Court to declare a person a delinquent director if such a person has conducted himself in a manner set out in section 162(5)(a) to (f).

In **Kruger v Kruger and Others (96886/2015) ZAGPPHC 1277 (8 December 2017)** Pretorius J made a finding that the first respondent was not only guilty of negligence but of wilful misconduct in respect of the performance of her function of director. The learned Judge stated at paragraph 38: "Accordingly, I have no choice, but to declare her as a delinquent director". Section 162(5)(c) does not give a Court discretion to refuse to make a delinquency order if the requirements of section 162(5)(c) are satisfied.

[16] The First Respondent tried to justify his conduct on the ground that his relationship with the Applicant had become strained and that the Applicant had himself neglected the affairs of the company and thus acted in dereliction of his duties to the company too. There is no merit in the First Respondent's socalled grounds of justification.

In the case of **Kukama v Lobelo and Others (38587/2011) South Gauteng High Court**, delivered on 12 April 2012 it was said:

"[20] Notwithstanding the strained relationship between the applicant and the first respondent as both directors and the shareholders of the second and third respondents, the legal obligations of a director bound the first respondent to discharge his duties in the same manner that it should, had the relationship between the two been normal."

Furthermore in the case of **Msimang NO and Another v Katuliiba and Others [2013] 1 All SA 580 (GSJ)** at paragraph 64 it was held that:

"However that Mavuso Msimang also acted in dereliction of his duties to the company, during the period between 2004 – July 2009, does not absolve Katuliiba and Mdwaba from failing to carry out their duties to the company."

[17] Of importance in the case of **Msimang NO and Another v Katuliiba and Others, supra**, Kathree – Setiloane J found:

"Section 162 of the new Companies Act provides that directors can be declared "delinquent" or "under probation" on various grounds, and on application by certain categories of applicant. This provision is directed at protecting companies and corporate stakeholders against company directors, who have proven themselves to be unable to manage the business of the company or have failed in, or are in neglect of, their duties and obligations as directors of a company."

In my view the conduct of the First Respondent in his dealings with the affairs of the Second Respondent Company in the present case did not measure up to the standard required and expected of a director and was in breach of his fiduciary duties to the company. The First Respondent's conduct fall short of the standard expected of a director of the Second Respondent Company to such an extent that it amounts to wilful misconduct, breach of trust and a gross abuse of his position as a director.

[18] It is trite that the defences open to a fiduciary who breaches his trust are very limited. Only the free consent of the principal after full disclosure will suffice. See **Phillips v Fieldstone Africa (Pty) Ltd and Another 2004 (3) SA 465 (SCA) at paragraph 31**.

[19] The First Respondent has launched a counter application for the liquidation of the Second Respondent Company on the basis that a deadlock has been reached and that it is just and equitable that the company be liquidated.

I am of the view that on the facts of the present case the First Respondent has not made out a case for the relief sought.

In **Emphy and Another v Pacer Properties (Pty) Ltd 1979 (3) SA 363 (D)** it was held that an applicant for such an order must not be wrongfully responsible for the situation that has arisen and that a deadlock does not per se entitle an applicant to a winding up under the just and equitable provision.

In **Mouw v Imanu – Shalom Congregation and Another 1994 (2) SA 240 (W)** it was held that a winding up order is not usually appropriate where there is an effective remedy against individual wrongdoers – the sharp instrument was preferred.

[20] In the present case the situation that has arisen and gave rise to the present proceedings was due to the undesirable conduct of the First Respondent. The effective remedy in the circumstances is therefore a delinquency order and not a winding up order.

Conclusion

[21] The First Respondent's conduct not only amounts to a serious breach of his fiduciary duty as a director of the Second Respondent but also to a breach of trust in relation to the continued performance of his director's functions within the Second respondent. He grossly abused his position as a director of the Second Respondent. There can be no justification for the First Respondent's aforesaid conduct.

The relief sought in the Notice of Motion is warranted as an absolute necessity to protect the Second Respondent, its clients and creditors as well as the Applicant from the First Respondent unlawful conduct.

[22] In view of the effect of an order declaring a director delinquent, it is in my view, not necessary to also order the First Respondent's removal as a director of the company due to the automatic inherent effect of such a declaration.

[23] I accordingly grant the following order:

23.1. The First Respondent is declared a delinquent director in terms of the provisions of section 162(5) of the Companies Act 71 of 2008.

23.2. The counter application for winding up or liquidation of the Second Respondent is dismissed.

23.3. The First Respondent is ordered to pay the costs of this application and counter application on the scale as between attorney and client.

E M MAKGOBA
JUDGE PRESIDENT OF THE HIGH COURT, LIMPOPO DIVISION, POLOKWANE

APPEARANCES

Heard on	: 28 November 2019
Judgment delivered on	: 23 January 2020
For the Applicant	: Ms M C De Klerk
	DDKK Attorneys Inc
For the First Respondent	: Adv J P Morton
Instructed by	: Charles Pieterse Attorneys
	c/o Thomas Grobler Attorneys