

REPUBLIC OF SOUTH AFRICA



**IN THE HIGH COURT OF SOUTH AFRICA
GAUTENG DIVISION, JOHANNESBURG**

CASE NO:2023-110502

(1)	REPORTABLE: NO
(2)	OF INTEREST TO OTHER JUDGES: NO
(3)	REVISED: NO
	<u>24 January 2025</u>
SIGNATURE	DATE

In the matter between:

FORTY SQUARES (PTY) LTD
MOGAMAT JASSEN DAVIDS
MOGAMAT FAJEK DAVIDS

First Plaintiff / Respondent
Second Plaintiff / Respondent
Third Plaintiff / Respondent

and

GL PALMER & COMPANY

Defendant / Applicant

JUDGMENT

Delivered: This judgment was prepared and authored by the Judge whose name is reflected on 24 January 2025 and is handed down electronically by circulation to the

parties/their legal representatives by e-mail and by uploading it to the electronic file of this matter on CaseLines. The date for hand-down is deemed to be 10h00 on 24 January 2025.

MALUNGANA AJ

- [1] The three plaintiffs instituted a delictual action against the defendant, a firm of chartered accountants, in which they seek payment of R62,237, 984.50 and R12, 527,049 respectively, for damages arising out of the defendant's professional negligence.
- [2] The defendant has taken exception to the particulars of claim on the basis that they are vague and embarrassing and, alternatively they lack the necessary averments to sustain the cause of action.
- [3] Before dealing with the defendant's grounds of exception, I find it apposite to sketch out the salient averments made by the plaintiffs in advancing the aforementioned claims:
- (i) In 2018 the defendant was contracted by Noris Fresh Produce (Pty) Ltd ("Noris") to perform the latter's annual audit for the year ending February 2018.
 - (ii) At the end of August 2018, the defendant delivered its audited report to Noris. The report is shown in annexure "POC1" of the particulars of claim.
 - (iii) According to the defendant, Noris' annual financial statements, presented fairly, in all material respects, the financial position, statement of comprehensive income, statement of charges in equity and statement of cash flows of Noris for the year ended 28 February 2018.
 - (iv) The financial statements audited by the defendant, and which the defendant stated in its report were, in all material respects, presented fairly Noris' financial position and income, recorded that Noris' revenue for the financial year ended 28 February 2018, was R1,397,500,863.00.

- (v) In performing its duties and preparing its report, the defendant acted negligently a aforesaid figures were false and incorrect and as the result of transfers of stock between various branches of Noris which were recoded as sales when they were in fact not. The correct revenue figure for the year ended 28 February 2018, was in fact R1,035,360,075.00.
- (vi) The plaintiff avers that the defendant, in conducting the audit of Noris' annual financial statements for the relevant year, did not do so with the requisite professional and reasonable skill and care.
- (vii) The defendant knew, or ought to have reasonably known the directors of Noris intended to use the report to induce the first plaintiff into purchasing all the issued shares in Noris, at a price based on the report.
- (viii) Further, the defendant knew, or to have reasonably known that the plaintiffs would rely on the opinion, report or statement in concluding the agreement with third parties, in relation to the purchase of shares in Noris.
- (ix) Relying on the defendant's report and the correctness of its contents
 - (a) The first plaintiff purchased the shares in Noris on or after May 2020;
 - (b) The first plaintiff advanced the amount of R12,527,049.00 to Noris pursuant to the first plaintiff's purchase of the shares in Noris, and
 - (c) The Plaintiffs bound themselves as sureties for Noris, for all amounts owed by Noris to Mercantile Bank, now owned by Capitec Bank Limited ("Capitec") arising from the purchase of the shares in Noris.
- (x) Had the plaintiff been aware of the correct revenue figures, they would not have committed the acts set out in paragraph 12 of the particulars of claim.

- (xi) The defendant owed the plaintiffs a duty to warn it that the report was incorrect, alternatively that the audit was not properly conducted.
- (xii) The defendant failed to issue such warnings, which failure was negligent and constituted a representation within the meaning of the Audit Profession Act 26 of 2005, to the effect that the financial statements were accurate and fairly presented as the financial position of Noris at the end of February 2018.

[4] I now turn to the grounds of exception. According to the excipient's heads of argument, there are two grounds of exceptions. The first ground relates to the plaintiffs' averments to the effect that defendant owed them a legal duty to warn them if the auditor's report was incorrect, alternatively to warn it if the audit was not properly conducted. In this regard the defendant states that if it were negligent and caused the plaintiffs' loss, such conduct is not wrongful, in that auditors do not owe a legal duty to third parties or companies or buyers entering into transactions with other third parties.

[5] In respect of the two amounts claimed as damages arising out of the negligence of the defendant, the defendant states that there is no logical or casual connection between the Defendant allegedly furnishing an incorrect report and;

(a) the first plaintiff purchasing the shares in Noris;

(b) more specifically, the plaintiff advancing the amount of R12 527 049.00.

(c) even more specifically, the plaintiffs binding themselves as sureties for Noris for all amount owed by Noris to Mercantile Bank, now owned by Capitec Bank Limited arising out of the purchase of the shares in Noris, and being allegedly liable for amounts allegedly owed by Noris to Capitec.

- [6] The defendant further complained that the plaintiffs do not plead that the amount paid by the first plaintiff to Noris in the sum of R12 527 049.00 was in respect of the purchase price, but merely allege it as “an amount paid by the first plaintiff to Noris.”
- [7] Under the circumstances, the defendant alleges that the particulars of claim fail to disclose the cause of action; alternatively, are vague and embarrassing.
- [8] Citing *Axiam Holding v Deloitte & Touche* 2006(1) SA 237 (SCA) at para 8, the defendant submitted that the auditors are only accountable to the companies they audit and not the shareholders or the employees of such company. It is not liable to buyers entering into transactions with the company. Such liability would be too remote to accrue.
- [9] The next basis upon which the defendant contends that it does not owe the plaintiff any legal duty is referred to in the case of *Cape Empowerment Trust Ltd v Fisher Hoffman Sithole* 2013 (5) SA 183 (SCA) at para 21 which dealt with the element of wrongfulness in the context of pure economic loss. The Court held the following:

“ ...as opposed to a loss of resulting from injury to person or property- wrongfulness is not presumed. More is needed. Considerations of public and legal policies dictate whether FHS should be held liable for the loss resulting from the misstatements of whether it should be afforded legal immunity. ...With reference to these considerations of policy some categories have been crystallized where legal liability for pure economic loss will be imposed as a matter of course (see eg. *Telematrix* para [15]; *Fourways Haulage SA (Pty) Ltd v SA National Roads Agency Ltd* 2009 (2) SA 150 (SCA) para[21]. But negligent misstatement by an auditor is not one of those.

None of these authorities, incidentally, mention the degree of negligence as one of the considerations and, for the reason given, I believe rightly so. Two considerations they do mention as relevant in the context of negligence misstatements are, first, whether the representation was made in the business context and in response to a serious request and, secondly, whether the Plaintiff

was dependent upon the defendant to provide the information or advice sought.”

[10] The defendant submitted that the two last considerations stated above were not pleaded by the plaintiffs. Counsel for the defendant argued further that there is no logical or legal connection between the defendant furnishing an incorrect report and the plaintiff purchasing the Noris shares or the first plaintiff advancing the amount of R12 527 049.00 to Noris.

[11] The Plaintiffs on the other hand, submitted that the defendant’s exception is based on the misunderstanding of the plaintiffs’ claim. It construed the plaintiffs’ case as one where the opinion of the auditor is sent out to the world upon which the third party places reliance. In actual fact, counsel for the plaintiffs argued that the auditor in the present case knew and/or ought to have known that an opinion expressed in respect of annual financial statements of the company would be utilized by shareholders of that company in negotiating a sale agreement with a purchaser, and would determine the purchase price to be paid in respect of that sale transaction. Properly interpreted, the case pleaded by the plaintiffs establishes that the defendant’s conduct was the cause of damages suffered by the plaintiffs.

[12] In arguing the issue of wrongfulness in relation to negligence, counsel for the plaintiffs cited *Hlumisa Investment Holdings RF Limited and Another v Kirkinis and Others* [2020]JOL 47567 (SCA) in which the Court held at 61 as follows:

“[61] In *Standard Chartered Bank of Canada v Nedperm Bank Ltd* 1994 (4) SA 747 (A) this Court had regard to the context in which the alleged negligent misstatement in that case was made, the purpose for which it was sought and made, the reliance placed on it by the third party, the relationship between the parties and finally and significantly for present purposes, public policy and fairness, and significantly for present purposes, public policy and fairness. It is true that *Axiam*, having regard to those factors, it was held that the question of wrongfulness could not be decided at exception stage. The minority in *Axiam* held that the exception ought to have been upheld. As in *Standard Chartered*

Bank, this Court in *Axiam* did not find any policy factors that militated against a finding at that stage against the auditors being held liable. The facts in *Standard Chartered* and *Axiam* are far removed from the facts in this case. In *Axiam* the question was whether the auditors of one company owed legal duties to other companies, who were in the process of negotiating agreements for share purchases and business financing and for this purpose relied on the audit statements and opinion which allegedly misrepresented the company's financial position. In both cases there was no claim by shareholders based on a diminution in share value."

[13] As in *Axiam Holdings v Deloitte & Touche* [2005] 4 All SA 157 (SCA), 2006 (1) SA 237 (SCA) (1 June 2005), the plaintiffs submitted that the appropriate time for the Court to assess an exception of this nature is at the trial where a full factual matrix will be placed before the Court.

[14] It is trite law that an exception that a cause of action is not disclosed by a pleading cannot succeed unless it be shown that *ex facie* the allegations made a plaintiff and any document upon which his or her cause of action may be based, the claim is (not may be) bad in law.¹

[15] A delictual action for pure economic loss would arise if, in the words of Corbett CJ in *Beyer South Africa (Pty) Ltd v Frost* 1991 (4) SA 559 (A) at 568B: '(i) the defendant or someone for whom the defendant is vicariously liable made a misstatement to plaintiff, (ii) that in making the misstatement the person concerned acted (a) negligently and (b) unlawfully (iii) the misstatement caused the plaintiff to sustain loss and (iv) that the damage claimed represent proper consideration for such loss.'²

[16] It is the duty of the excipient to persuade the court that upon every interpretation which in the particulars of claim including the contract between the parties, can reasonably bear, no cause of action is disclosed.³

¹ Vermeulen v Goose Valley Investments (Pty) Ltd 2001 (3) SA 986 (SCA) at 997,

² Van Zyl NO v Kantey & Templer (Pty) Ltd [2005] 4 All SA 225 (C)

³ Lewis v Oneanate (Pty) Ltd and Another 1992 (4) SA 811(A) at 817F-G).

- [17] It is averred in the particulars of claim (paragraph 11), that when the defendant prepared the report knew and ought to have reasonably known that Noris directors intended to use it, including annual financial statements in respect of which the report was to induce the first plaintiff into purchasing all the issued shares in Noris, as at the price based on the report.
- [18] As a point of departure it is instructive to have regard to section 46 (3) of the Auditing Profession Act, 26 of 2005 ('the Act'). It provides that a registered auditor incurs liability to third parties who have relied on an opinion, report or statement of that registered auditor for financial loss suffered as a result of having relied thereon, only if it proved that the opinion was expressed or the report or statement was made, pursuant to a negligent performance of the registered auditor's duties and registered auditor- (a) knew, or could in particular circumstances reasonably have been expected to know, at the time when the negligence occurred in the performance of the duties pursuant to which the opinion was expressed or the report or statement was made.
- [19] A copy of the defendant's audit report or financial statement, which the plaintiffs' claim is predicated upon is shown in the plaintiff's particulars of claim as annexure "POC1".
- [20] A close scrutiny of the Act, defines a "third party" as "any person other than a client." It follows that if a third party, the plaintiff in this case, is able to establish a legal duty within the ambit of section 46(3) of the Act, then the auditor in question would incur liability. In terms of section 46(7) of the Act, an auditor may also incur liability to a shareholder, creditor or investor of an entity if the auditor fails to report a reportable irregularity in accordance with section 45.
- [21] Having regard to the provisions of section 46 of the Act and the averments contained in the plaintiffs' particulars of claim it cannot be said at this stage of the exception, that the particulars of claim do not disclose the cause of action. Much of what has been pleaded by the plaintiffs are plainly matters for evidence, which can be properly ventilated at the trial by way of evidence. As in *Standard Chartered Bank of Canada* supra, the court will consider the context within which

the alleged negligent misstatement were made, the purpose for which is was made, and the reliance placed upon the report by the plaintiffs.

[22] As regards the issue of costs, this was substantially a complex matter. That being the case, a successful party is entitled to costs at Scale C.

Order

[23] The exception is dismissed with costs, such costs to include the costs of senior counsel.



MALUNGANA AJ
ACTING JUDGE OF THE HIGH COURT
JOHANNESBURG

Heard on: 31 October 2024

Delivered on: 24 January 2025

For the Applicant: Adv C Georgiades SC instructed by Messina Incorporated

For the Respondent: Adv D van Reenen instructed by Fullard Mayer Morrison Inc

