CURBING THE ABUSE OF THE TRUST FORM: THE INCLUSION OF PENALTY AND PROHIBITION PROVISIONS AS WELL AS COMPULSORY AUDITS IN THE TRUST PROPERTY CONTROL ACT 57 OF 1988

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Abstract

The abuse of the trust form has become prevalent in recent times. As a consequence our courts have relied on other branches of law to find remedies to assist third parties who contract with trusts. This article analyses some of these remedies, as well as amendments to the Trust Property Control Act which could provide assistance in combating the abuse of the trust form. There are, however, certain remedies which should continue being developed by our courts.

Keywords:

Abuse of trust form, alter ego trust, piercing the trust veneer, Trust Property Control Act, penalty and prohibition provisions, compulsory audits

1 Introduction

The South African Law Reform Commission ("SALRC") in its Report ("SALC Report")[1] on trusts expressed its opposition against the inclusion of penalty provisions in the proposed Trust Property Control Act 57 of 1988 ("TPCA"). However, with the increase in the number of cases where an abuse of the trust form occurred, the question that will be addressed in this article is whether the TPCA should be amended to include penalty provisions and a so-called prohibition against reckless behaviour, as well as requiring compulsory audits, to combat this problem. The article will, first, highlight

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1 South African Law Commission *Review of the Law of Trusts Project 9* Report (1987). (At the time the report was issued, the Commission was known as the South African Law Commission ("SALC") and therefore this acronym will be used throughout. The Judicial Matters Amendment Act No 55 of 2002 changed the Commission's name to the South African Law Reform Commission.

the reasons why the SALC opposed the inclusion of penalty provisions. This will be followed by an analysis of recent cases where an abuse of the trust form occurred as a consequence of trustees' non-compliance with the TPCA, their common-law duties, and/or their duties in terms of the relevant trust deed. It will be argued that these cases evince the need for the amendment of the TPCA as they do not always provide adequate remedial relief. Lastly, recommendations and proposals will be made on the content of such amendments.

2 The SALC's reasons for opposing the inclusion of penalty provisions

While acknowledging that it is customary to make non-compliance with a statutory provision that is generally of an administrative nature punishable as an offence, the SALC felt that it would be undesirable to apply criminal sanctions in an area where civil remedies and administrative procedures already exist. The SALC felt that doing so would result in the unnecessary criminalisation of conduct.[2] What these available civil remedies and administrative procedures are, is not apparent from the SALC Report.

It should, however, be highlighted that at the time the SALC Report was published, the current problems that our courts face relating to the abuse of the trust form were not as common. The case law on the abuse of the trust form strengthens the argument that the SALC's reasoning as to why penalty provisions should not be included is no longer justified. To assist third parties who contract with a trust in those instances where the trustee(s) abuse the trust form, the courts have sought recourse in other branches of law. These remedies will be analysed later. However, the application of these remedies often depends on the facts.

3 Abuse of the trust form

In *Land and Agricultural Bank of South Africa v Parker* ("*Parker*"),[3] the Supreme Court of Appeal ("SCA") noted that the core idea of a trust is the separation of ownership (control) from enjoyment.[4] Such separation, *inter alia*, ensures diligence on the part of a trustee.[5] A lack of separation between control and enjoyment invites an abuse of the trust form.[6] An abuse of the trust form occurs in those instances where the trustees, in essence,

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2 95.

3 2005 2 SA 77 (SCA).

4 Para 19. See also *REM v VM* 2017 3 SA 371 (SCA) para 19; *Van Zyl v Kaye* 2014 4 SA 452 (WCC).

5 *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) para 22.

6 E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 2 ed (2018) 308.

fail to adhere to their core duties of trust administration.[7] According to De Waal,[8] the core duties of trustees are: trustees must exercise an independent discretion; trustees must give effect to the trust deed; and trustees must, in the performance of their duties and exercise of their powers, act with care, diligence, and skill. In *Van der Merwe v Hydraberg Hydraulics CC, Van der Merwe v Bosman*[9] the court stated that an abuse of the trust form should not be countenanced lightly, especially where the facade of a trust is used to protect the trustees against fraud, dishonesty, and unscrupulous defences against *bona fide* third parties.

While beneficiaries of a trust have an action for breach of trust against a trustee if they can show that they sustained patrimonial loss as a consequence of a trustee's conduct,[10] a third party does not, as it is not a party to the fiduciary relationship between a trustee and beneficiary. Furthermore, the remedy of a removal request which is available in the TPCA for third parties (as well), does not assist. Consequently, as mentioned earlier, our courts have sought remedies in other branches of law to assist in instances where a third party has contracted with a trust and an abuse of the trust form occurred. In *Parker*,[11] the SCA took the opportunity to address the issues pertaining to the abuse of the trust form and suggested certain remedies that may be used to alleviate the consequences flowing from a lack of separation between enjoyment and control.[12] The following were the remedies proposed: reliance on the *Turquand* rule; reliance on agency principles; piercing the veneer of the trust veil; and the appointment of an independent trustee by the Master.

4 Remedies proposed by the Supreme Court of Appeal

4.1 *Turquand* rule

The *Turquand* rule was applied to trusts for the first time in *Man Truck & Bus (SA) Ltd v Victor*.[13] In *Vrystaat Mielies (Edms) Bpk v Nieuwoudt*,[14] the court

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7 See F Du Toit, BS Smith & A van der Linde *Fundamentals of South African Trust Law* (2019) 139.

8 MJ De Waal "The Abuse of the Trust (or: 'Going Behind the Trust Form') – The South African Experience with Some Comparative Perspectives" (2012) *Rabel J* 1095. See also ch 7 in Du Toit et al *Trust Law*; ch 6 in Cameron et al *Law of Trusts*.

9 2010 5 SA 555 (WCC) 568E-571H. See *Ex Parte Gore* 2013 3 SA 382 (WCC) for the court's explanation of the term "unconscionable abuse" in s 20(9) of the Companies Act 71 of 2008.

10 See *Jowell v Bramwell-Jones* 1998 1 SA 836 (W). *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) para 22 notes that a lack of separation between control and enjoyment may be visited with action by beneficiaries. See also Du Toit et al *Trust Law* 184.

11 2005 2 SA 77 (SCA).

12 88B-C; Cameron et al *Law of Trusts* 308.

13 2001 2 SA 562 (NC). F du Toit "Jurisprudential Milestones in the Development of Trust Law in South Africa's Mixed Legal System" in L Smith (ed) *The Worlds of the Trust* (2013) 265-266 regards this decision as an "innovation". See also JS McLennan "Contracting with Business Trusts" (2006) 18 *SA Merc LJ* 330, who observes that the judge attempted to make legal history.

14 2003 2 SA 262 (O).

stated that, although a trust is not a legal person, there was no reason why the rule could not be applied to the matter at hand. To hold otherwise would amount to a breach of good faith that should exist between contracting parties.[15] Thus, the application of the *Turquand* rule was regarded as a necessity.[16]

However, on appeal, the applicability of the rule to trusts was left open.[17] It was noted by Farlam JA (on behalf of the majority) that the rule could not be used as the trust deed's clause in question only applied to the signing of documents for "official purposes" and not to the type of contract signed by the first appellant.[18] No specification of the type of documents which would fall within the "official purposes" category was provided,[19] thereby rendering this finding questionable and creating the impression that Farlam JA indirectly denounced the application of the rule to trusts.

Harms JA, in a concurring judgment, highlighted certain problems associated with trusts, one of them being that there is no central register for trusts or trustees as there is for companies and close corporations.[20] A member of the public would have to determine first where the trust deed was lodged. Thereafter, an application to the Master for permission to inspect the trust deed would have to be made, which the Master, in exercising his discretion, could refuse. Consequently, the underlying principle of the *Turquand* rule would be difficult to apply to trusts.[21] Furthermore, third parties cannot simply assume that a trustee has the necessary authority.[22]

Be that as it may, it is submitted that the *Turquand* rule could find application if a trust deed allows for delegation.[23] Outsiders dealing with trusts have no means of ascertaining whether delegation by resolution took

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15 267H-I.

16 268C-D.

17 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) 493D.

18 492A-B and 492D.

19 HGJ Beukes "Does the Turquand Rule Apply to Internal Requirements in a Trust Deed?" (2004) 16 *SA Merc LJ* 269 argues that it is not apparent why the signing of an agreement that falls within the business sphere of a trust and which is signed on behalf of a trust cannot be regarded as the signing of a document for official purposes. Thus, she contends that the clause indeed formed the basis for the application of the *Turquand* rule since it provided for the potential authority of one of the trustees to bind the trust.

20 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 493H. See also *Van der Merwe v Hydraberg Hydraulics CC, Van der Merwe v Bosman* 2010 5 SA 555 (WCC) 566B-C.

21 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) 494B-C. See also *Van der Merwe v Hydraberg Hydraulics CC, Van der Merwe v Bosman* 2010 5 SA 555 (WCC) 566C-D.

22 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) 494G. This is in line with the decision in *Wolpert v Uitzigt Properties (Pty) Ltd* 1961 2 SA (W) 264B-C, where it was stated that a third party cannot assume that the person professing to act indeed had the necessary authority, especially if the act is outside the usual scope of authority. In such instance, a third party would have to enquire further to ensure that the official has actual authority or elicit facts which would estop the company from denying such authority.

23 McLennan (2006) *SA Merc LJ* 331 considers that delegation is not simply about whether it is possible in terms of the trust deed, but rather whether actual delegation took place or the established facts preclude a company from denying that it took place.

place, as resolutions need not be lodged with the Master.[24] The application of the rule in this instance would be a means of avoiding the consequences that would ensue if the trustees were to rely on non-compliance with the joint-action rule for the trust to escape liability.[25]

De Waal and Du Plessis propose that a provision such as that contained in section 7 of the Trusts (Scotland) Act of 1921 ("Trusts (Scotland) Act") would assist in combating the current difficulties where an abuse of the trust form has occurred.[26] Section 7 provides:

> "Any deed bearing to be granted by the trustees under any trust, and in fact executed by a quorum of such trustees in favour of any person other than a beneficiary or a co-trustee under the trust where such person has dealt onerously and in good faith shall not be void or challengeable on the ground that any trustee or trustees under the trust was or were not consulted in the matter, or was or were not present at any meeting of trustees where the same was considered, or did not consent to or concur in the granting of the deed, or on the ground of any other omission or irregularity of procedure on the part of the trustees or any of them in relation to the granting of the deed."

The authors contend that this provision has the same effect as the *Turquand* rule[27] and certainly would safeguard third parties.

In *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* ("*Nieuwoudt*"), Harms JA stated that whether trustees have acted in a particular manner is not a matter of internal management, but rather one determining the scope of their authority.[28] Third parties, therefore, cannot assume that trustees have the

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[24] See JS McLennan "The Ultra Vires Doctrine and the Turquand Rule in Company Law – A Suggested Solution" (1979) 96 *SALJ* 346, where the author observes that an inspection of the company's public documents will not enlighten a third party as to whether or not delegation in fact took place. MJ Oosthuizen "Die *Turquand*-reël as reël van die Verenigingsreg" (1977) *TSAR* 210-219 also shows that the rule is not dependent on the legal personality of the association or the applicability of the doctrine of constructive notice and thus argues that the rule can apply to institutions that are not bestowed with legal personality and to which the doctrine of constructive notice does not apply. While resolutions need not be lodged with the Master, obtaining the resolution from trustees may be possible.

[25] See F du Toit "Die Aanwending van die *Turquand*-reël in die Suid-Afrikaanse Trustreg" (2004) *TSAR* 150-161. According to H Claasen "Aanwending van die Turquand-reël in die Trustreg" (2004) *De Rebus* 25, a third party could invoke the rule if he transacts with the board of trustees or the managing trustee, if there is one. The rule, according to the author, would not assist in the instance where a third party deals with an ordinary trustee. In such a situation, a third party would have to inquire further.

[26] MJ de Waal & I du Plessis "A Comparative Perspective on the 'Joint-action Rule' in the Context of Business Trusts" (2014) *Stell LR* 359.

[27] De Waal and Du Plessis (2014) *Stell LR* 359.

[28] *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) 494E. See *Bester v Richter, Niewoudt, Malherbe, Geldenhuys, Conradie, Kellerman, Conradie, Visser, Horn, Visser* (7596/2015, 11901/2015, 11210/2015, 11321/2015, 11229/2015, 11209/2015, 11233/2015, 11208/2015, 11641/2015, 11211/2015) [2015] ZAWCHC 169 (6 November 2015) *SAFLII* para 34 <http://www.saflii.org/za/cases/ZAWCHC/2015/169.html> (accessed 10-08-2020) where the court states that our law may well develop to ensure the application of the *Turquand* rule in certain

necessary authority. Although a provision similar to section 7 of the Trusts (Scotland) Act would run contrary to this view and would also be in conflict with the joint-action rule, which requires that trustees act jointly unless the trust deed stipulates otherwise,[29] it is nonetheless submitted that the frequency with which trustees use deficiencies in authorisation, as well as their lack of compliance with the joint-action rule, to escape liability, as evident from case law, necessitates the incorporation of a similar provision into the TPCA. It is submitted that such a provision will safeguard the interests of third-party contractants with trustees; moreover, reliance on the *Turquand* rule (as with many of the other remedies to be analysed below) would become unnecessary. It is proposed, therefore, that, as recommended by De Waal and Du Plessis, a provision akin to section 7 of the Trusts (Scotland) Act be included in the TPCA. The recommendation is as follows:

> Any contract concluded by a quorum of trustees under any trust, with any person other than a beneficiary or a co-trustee under the trust and which such person concluded onerously and in good faith shall not be void or challengeable on the ground that any trustee or trustees under the trust was or were not consulted in the matter, or was or were not present at any meetings of trustees where same was considered, or did not consent or concur in the conclusion of the contract, or on the ground of any other omission or irregularity of procedure on the part of the trustees or any of them in relation to the conclusion of such contract.[30]

4.2 Ostensible authority (estoppel) and implied warranty of authority

In *Nieuwoudt*, Harms JA considered that the ordinary principles of agency could apply to trusts where a trustee expressly or by implication authorised someone to act on his behalf.[31] In such instance, a third party could rely on that trustee acting on the ostensible authority of the other trustees. However,

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circumstances. *Cf* Du Toit et al *Trust Law* 110 who submit that the *Nieuwoudt* and *Van der Merwe v Hydraberg Hydraulics CC, Van der Merwe v Bosman* cases shut the door to the application of this rule to trusts.

29 See *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) 493E; *Smit v van der Werke* 1984 1 SA 164 (T) 174B-D; *Cooper v The Master* 1996 1 SA 962 (N) 967H; *Thorpe v Trittenwein* 2007 2 SA 172 (SCA) 176H; *Lupacchini v Minister of Safety and Security* 2010 6 SA 547 (SCA) 459D; *Northview Shopping Centre (Pty) Ltd v Revelas Properties Johannesburg CC* 2010 3 SA 630 (SCA) 634D-E, with reference to *Thorpe v Trittenheim supra*; *Steyn v Blockpave (Pty) Ltd* 2011 3 SA 528 (FB) 530B-C; *O'Shea v Van Zyl* 2012 1 SA 90 (SCA) 97B; *Pascoal v Wurdemann* 2012 2 SA 422 (GSJ); *Bonugli v Standard Bank of South Africa Ltd* 2012 5 SA 202 (SCA) 207F; *Meijer v Firstrand Bank Limited (Formerly Known as First National Bank of Southern Africa) in re Firstrand Bank Limited (Formerly Known as First National Bank of Southern Africa) v Meijer* [2013] JOL 30560 (WCC) [11].

30 Author's recommendation for the wording of an additional provision to the TPCA.

31 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) 494H-I.

whether the trustee had ostensible authority is a matter of fact and not one of law.[32]

As to whether ostensible authority exists, the requirements laid down in *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* would have to be met:[33] there must be a representation by words or conduct; the representation was made by the principal, and not the agent, that the agent had the authority to act as he did; the representation must be of such a form that the principal reasonably should have expected that outsiders would act on it; there was reliance by a third party on the representation; the reliance on the representation was reasonable; and there was consequent prejudice to the third party.[34]

Also, a third party must heed the additional statements made by the SCA in *Glofinco v Absa Bank Ltd* relating to limitations on ostensible authority.[35] The principles pertaining to ostensible authority are well established in the common-law and thus incorporating these requirements, as mentioned above, into the TPCA under the rubric of protecting third-party interests is not necessary.

Reliance can be placed on another agency principle. Harms JA in *Nieuwoudt* noted that a trustee could be held liable personally for breaching a warranty of authority.[36] An implied warranty of authority refers to the situation where an undertaking is made that the representation is correct. Thus, if the statement subsequently turns out to be incorrect, a breach of an implied warranty of authority will have occurred.[37]

To rely on this remedy, a third party will have to show: first, that the agent represented that he had authority; secondly, that the agent's representation induced the third party to enter into the contract; thirdly, that the agent did not have authority; and fourthly, that as a result of the principal not being bound, the third party suffered loss.[38]

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32 494I-J.

33 *NBS Bank Ltd v Cape Produce Co (Pty) Ltd* [2002] 2 All SA 262 (A) para 25.

34 Para 26. See also *South African Eagle Insurance Co Ltd v NBS Bank Ltd* 2002 1 SA 560 (SCA); *South African Broadcasting Corporation v Coop* 2006 2 SA 217 (SCA); *Oppex Consultants CC v University of KwaZulu-Natal* (1053/08) [2012] ZAKZDHC 30 (1 June 2012) *SAFLII* <http://www.saflii.org/za/cases/ZAKZDHC/2012/30.html> (accessed 10-08-2020); *Absa Bank Ltd v Mahomed* 2014 2 SA 466 (SCA); *Gihwala v Grancy Property Ltd* 2017 2 SA 337 (SCA).

35 *Glofinco v Absa Bank Ltd t/a United Bank* 2002 6 SA 470 (SCA) 479F-483E.

36 *Nieuwoudt v Vrystaat Mielies* 2004 3 SA 486 (SCA) 495A. However, the judge emphasised that this remedy, depending on the circumstances, could be of little solace.

37 AJ Kerr *The Law of Agency* 4 ed (2006) 245.

38 *Blower v Van Noorden* 1909 TS 900. See also *Indrieri v Du Preez* [1989] 2 All SA 254 (C) 258-259, where the court elaborated on the liability of the would-be agent. In this regard, it was said that the liability that ensues is not liability to perform in terms of the contract. Instead, it is to place the other contracting party in as good a position as if the principal actually had been bound. Thus, a third party will have to establish not only what would have been payable under the contract, but also how much he would have been able to recover from the agent's principal had the principal been bound. Thus, for example, where a principal is insolvent or indigent, the claimable amount would be considerably less than the amount that would have been payable under the contract.

Since our courts have acknowledged the possibility of the remedy, it is submitted that it can be relied upon if the circumstances permit and if the requirements are met. Once again, this is a remedy that should be developed in the context of trusts by our courts and, therefore, should not, it is submitted, be regulated under the TPCA.

4.3 Going behind the trust form

Since a trust is not a legal person there is no "veil" to "pierce".[39] Notwithstanding the use of the words "veil" and "veneer" in the trust law context, our courts have confirmed on several occasions that the trust does not enjoy separate legal personality. Be that as it may, it has become evident that trustees hide behind the trust form in order to escape liability when they have abused the trust form. It is submitted that the more appropriate term for the remedy in this instance would be "going behind the trust form".[40]

In *Van Zyl v Kaye* ("*Van Zyl*"), the court considered the application of the doctrine of piercing the corporate veil in the context of trusts and provided clarity regarding instances of sham trusts as well as those where a court will have to go behind the trust form.[41] The court stated that if a trust is a sham, the remedy of piercing would be of no use since no trust has come into existence and, therefore, there is nothing to "go behind".[42] However, when a court goes behind the trust form, it is accepted that the trust exists, only for the usual consequences of its existence then to be disregarded. The consequence of such a finding could result in a trustee being held personally liable for an obligation ostensibly undertaken in his capacity as trustee, or in the trust being bound by the transactions ostensibly performed by the trustee acting

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The onus rests on the third party to establish the quantum of damages that could have been recovered from the principal had the principal been bound. This could explain Harms JA's statement that the remedy could be of little solace. See also *Miejer v Firstrand Bank Limited (Formerly Known as First National Bank of Southern Africa) in re Firstrand Bank Limited (Formerly Known as First National Bank of Southern Africa) v Meijer* [2013] JOL 30560 (WCC) paras 25, 27, 28 where it was said that a lack of authority may in appropriate circumstances be cured by ratification. The effect of a valid ratification would cloak an agent's unauthorised act with authority retrospectively. Ratification would, however, not be possible in the situation where a trust suffers due to an incapacity created by the non-compliance of a minimum number of trustees.

39 See *RP v DP* 2014 6 SA 243 (ECP) 248E.

40 See De Waal (2012) *Rabel J* 1085.

41 *Van Zyl v Kaye* 2014 4 SA 452 (WCC). See however, RB Stafford *A Legal Comparative Study of the Interpretation and Application of the Doctrines of the Sham and the Alter-ego in the Context of South African Trust Law The dangers of translocating company law principles into trust law* LLM thesis Rhodes University (2010) 68-178 for criticism of the courts' use of the *alter ego* doctrine and the doctrine of piercing the corporate veil in the trusts context. See *BC v CC* 2012 5 SA 562 (ECP) and *RP v DP* 2014 6 SA 243 (ECP) where the court conflated the law pertaining to sham trusts and alter ego trusts.

42 *Van Zyl v Kaye* 458E. A trust will be declared a sham if the court is satisfied that the requirements for the creation of a trust were not met or that the appearance of having met them was a simulation.

beyond the scope of his authority.[43] The remedy, it was said, is an equitable one, afforded to a third party affected by an unconscionable abuse of the trust form,[44] provided the circumstances so permit.[45] Here the epithet "equitable", according to the court,[46] relates to the remedy in its ordinary rather than its legal sense.[47] In other words, the remedy lends itself to a flexible approach that can fairly and justly combat the consequences of an unconscionable abuse of the trust form.[48] Generally, the remedy will be granted when the trust form is used in a dishonest or unconscionable manner to evade liability or avoid an obligation.[49]

It was noted by the court in *Van Zyl* that even if the conduct of the relevant trustee in administering the trust could be accepted as being illustrative of the trustee disregarding his fiduciary duties and treating the trust as his *alter ego*, his conduct still did not render the trust a sham.[50] However, according to the court in *Van Zyl*, the conduct of the trustee could lead to a trustee's removal; or an independent co-trustee being appointed; or a trustee being held liable personally for transactions ostensibly concluded on behalf of the trust; or a trustee being held liable delictually.[51]

It is evident that the test to be applied is to determine whether there was an unconscionable abuse on the part of the trustee(s). Whereas the Companies Act 71 of 2008 ("Companies Act") contains provisions governing the piercing of the corporate veil, it is submitted that cognate provisions should not be inserted into the TPCA, given the clarification that has emerged from the *Van Zyl* decision. Instead, principles pertaining to going behind the trust form should continue to be developed by our courts, since the statutory provisions governing piercing the corporate veil have generated further questions.[52]

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43 *Van Zyl v Kaye* 2014 4 SA 452 (WCC) 459G-460A.

44 460D-E; *REM v VM* 2017 3 SA 371 (SCA) para 17. See also Cameron et al *Law of Trusts* 311 who argue that unconscionability and dishonesty should not necessarily be seen as requirements before a trustee's conduct can be regarded as trust abuse; E Nel *An Interpretive Account of Unconscionability in Trust Law* (2014) *Obiter* 81 for an analysis of the term "unconscionability" in the trust law context.

45 *Van Zyl v Kaye* 2014 4 SA 452 (WCC) 460E.

46 But see the concerns raised by A van der Linde "Debasement of the Core Idea of a Trust and the Need to Protect Third Parties" (2012) *THRHR* 377-379.

47 To distinguish it from English law and to clarify that this is not a situation where courts are trying to incorporate English terminology. The court thus clarifies the questions raised by Van der Linde (2012) *THRHR* 377-379.

48 *Van Zyl v Kaye* 2014 4 SA 452 (WCC) 460F.

49 460F.

50 465G.

51 465G-H.

52 See R Cassim "Piercing the Corporate Veil: 'Unconscionable Abuse' under the Companies Act 71 of 2008" (2012) *De Rebus* 22-24; N Schoeman "Piercing the Corporate Veil under the New Companies Act: Is s 20(9) read with s 218 a Codification of the Common Law Concept or is it Further Reaching?" (2012) *De Rebus* 28. However, in R Cassim "Hiding behind the Veil" (2013) *De Rebus* 197 the author mentions that *Ex Parte Gore* 2013 3 SA 382 (WCC) clarified many of

Furthermore, it is likely that the absence of a definition for unconscionable abuse in the Companies Act is due to the realisation that no definition could encompass all types of unconscionable abuse. The courts, it is submitted, are best suited to determine whether an unconscionable abuse has occurred.

The submission that the principles of going behind the trust form should be developed by our courts instead of the legislature is strengthened by the controversial application of this remedy regarding claims to trust assets in divorce cases. In *Badenhorst v Badenhorst* ("*Badenhorst*")[53] the appellant sought that the court, in awarding a redistribution of assets order in terms of section 7 of the Divorce Act 70 of 1979 ("Divorce Act"), considers the assets of an *inter vivos* trust in addition to the respondent's personal estate on the basis that the trust was the respondent's (trustee's) alter ego. While the SCA acknowledged that the trust's assets did not form part of the respondent's personal estate, this did not bar the court from adding the value of the trust's assets to the value of the respondent's personal estate in its award of the redistribution order.[54] The consideration of the value of the assets of alter ego trusts featured in a number of subsequent judgments on the calculation of accrual claims[55] in divorce proceedings. In both *BC v CC*[56] and *RP v DP*[57] the courts held that the value of the trust assets can be taken into account in calculating a spouse's accrual claim. The courts did so because they regarded piercing the trust veneer to permit the consideration of the value of alter ego trust assets as a function of the common law that is not intrinsically bound to the judicial discretion inherent to the statutory redistribution dispensation under the Divorce Act. However, in *MM v JM,*[58] the court held that there is no legal basis for including trust assets in the calculation of an accrual claim because the Divorce Act's equitable and discretionary redistribution dispensation differs fundamentally from the Matrimonial Property Act's strictly mathematical calculation of accrual claims.[59] In *WT v KT* ("*WT*"),[60] the SCA concurred with the latter view when it stated (seemingly *obiter*), that unlike claims for the redistribution of assets which affords the court a discretion when awarding such claims, the same did not hold true with regard to claims where the parties are married in community of property or out of community of property subject to the accrual system. The SCA was, therefore, unwilling to extend the principles enunciated in the *Badenhorst*

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the issues raised in his 2012 article, but notes that it will be interesting to see how the statutory remedy will be developed further by the courts.

53 2006 2 SA 255 (SCA) 257H-258A.

54 260H.

55 In terms of s 3 of the Matrimonial Property Act 88 of 1984.

56 2012 5 SA 562 (ECP).

57 2014 6 SA 243 (ECP).

58 2014 4 SA 384 (KZP).

59 391F.

60 2015 3 SA 574 (SCA).

case to accrual claims and the division of joint estates in marriages concluded in community of property. The court placed particular reliance on section 12 of the TPCA that recognises that trust assets do not form part of the personal property of a trustee as a matter of law.[61] These judicial developments illustrate the potency with which South African courts can engage in settling the principles applicable to going behind the trust form in instances of the abuse of the trust. Indeed, Du Toit[62] notes that, regardless of the *WT* judgment, room still exists for future legal development in this regard. This much is evident from *REM v VM* ("*REM*")[63] in which the court confirmed that the remedy can be awarded in respect of marriages out of community of property subject to the accrual system in those instances where the trust form is used in a dishonest or unconscionable manner to evade a liability or to avoid an obligation.[64] A further issue addressed in the judgment was whether a spouse who is not a beneficiary, or a third party, has *locus standi* to challenge the management of the trust by the other spouse. The SCA in *REM* overrode its own decision in *WT* where the court held that such spouse did not enjoy *locus standi*.[65] In *REM* the SCA stated that it is illogical to distinguish between the legal standing of a third party who contracts with a trust and institutes a claim on that basis and a spouse who seeks to advance a patrimonial claim.[66] A contentious aspect of this judgment, however, is that a declaration can be made that trust assets be used to satisfy the particular claim.[67] While this aspect is beyond the scope of the article, it illustrates the need for our courts to continue developing rules pertaining to this remedy in the context of trusts.[68]

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61 584G-I. For a critique of the *WT* judgment, see C Marumoagae "Protecting Assets through a Discretionary Trust in Anticipation of Divorce" (2017) *Obiter* 34; BS Smith "Statutory Discretion or Some Common Law Power? Some Reflections on "Veil Piercing" and the Consideration of (the Value of) Trust Assets in Dividing Matrimonial Property at Divorce I" (2016) *JJS* 68; IM Shipley "Trust Assets and the Dissolution of a Marriage: A Practical Look at Invalid Trusts, Sham Trusts, and Piercing the Veneers of Trusts / Going Behind the Trust Form" (2016) *SA Merc LJ* 508; A van der Linde "Whether Trust Assets Form Part of the Joint Estate of Parties Married in Community of Property: Comments on 'Piercing of the Veneer' of a Trust in Divorce Proceedings *WT v KT* 2015 (3) SA 574 (SCA)" (2016) *THRHR* 165.

62 F du Toit "South Africa – Trusts and the Patrimonial Consequences of Divorce: Recent Developments in South Africa" (2015) *JCLS* 699-701.

63 2017 3 SA 371 (SCA). Du Toit et al *Trust Law* 158 highlight that the court in *REM* did not override the decision in *WT* regarding the application of the remedy to marriages in community of property.

64 *REM v VM* 2017 3 SA 371 (SCA) 380A. Note, however, BS Smith "Perspectives on the Juridical Basis for Taking (the Value of) Trust Assets into Account for the Purposes of Accrual Claims at Divorce: *REM v VM*" (2017) *SALJ* 723-727 who expresses concerns regarding the juridical basis for the piercing of the trust veneer remedy.

65 *WT v KT* 2015 3 SA 574 (SCA) 583F-584C.

66 *REM v VM* 2017 3 SA 371 (SCA) 379F-380A.

67 380C. See also Smith (2017) *SALJ* 723; Du Toit (2015) *JCLS* 687-688.

68 Room also exists for further development in the context of marriages in community of property: see Du Toit et al *Trust Law* 158

4.4 Independent trustee

In *Parker*, the SCA stated that the Master must ensure that in every trust, adequate separation of control from enjoyment is maintained.[69] This the Master could do by insisting on the appointment of an independent trustee to every trust where (a) the trustees are all beneficiaries, and (b) the beneficiaries are all related to one another.[70]

These concerns notwithstanding, the Acting Chief Master of the High Court attempted to align the registration of trusts and the appointment of trustees with the SCA's directive by means of Circular 2 of 2005, which amended the JM21E and Acceptance of Trusteeship forms. The Circular, however, reiterated that (a) each matter still is to be decided upon its own merits by taking into account all the information placed before the Master as well as adherence to the *audi alteram partem* rule; and (b) the Master still has a clear statutory discretion when it comes to the appointment of trustees.[71]

Since the Master already is empowered by virtue of his supervisory role over trusts, and since the Master in any event will exercise his discretion only after a consideration of all the facts, it is submitted that a provision regulating the appointment of an independent trustee need not be included in the TPCA. Furthermore, the Master's Directive 2/2017 ("Directive") sets out the Master's Office's attempt at giving effect to the *Parker* decision. The Directive deals with the description of a family business trust; who would "qualify" as an independent trustee; dispensing with the appointment of an independent trustee; as well as the nomination, remuneration, and resignation of an independent trustee.

5 Provisions governing other fiduciary functionaries

A trustee, similar to a director, does not stand in a fiduciary relationship to third parties.[72] Nevertheless, the Companies Act makes provision for third parties whereas the TPCA, in its current form, only affords third parties the option to request the removal of a trustee. Section 22(1) of the Companies Act, for example, contains a reckless trading prohibition clause. It provides: "A company must not carry on its business recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose."

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69 *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) 90A.

70 90A-B.

71 BS Smith "*Parker*, Life Partnerships and the Independent Trustee" (2013) *SALJ* 528.

72 See *WT v KT* 2015 3 SA 574 (SCA) 583E-F. *Cf REM v VM* 2017 3 SA 371 (SCA) 379C where the court stated that trustees owe a fiduciary responsibility to a spouse who is not a trustee and/or third party. This brings to the fore the following question: can the non-beneficiary spouse and/or third party sue on the basis of breach of trust? If so, this will negate the need for the transposition of the various remedies to trust law.

It is submitted that a similar provision should be incorporated into the TPCA.[73] A failure by a trustee to comply with trust administration principles could fall within the category of recklessness, gross negligence or even fraud (the latter where a trustee alleges that he has authority to bind the trust while knowing that he does not). If a third party can illustrate that a trustee's conduct fell within one of the listed categories, the remedy should be afforded to such third party. It is evident from the case law involving business trusts that the TPCA in its current form does not effectively protect third parties. While our courts are indeed extending remedies from other branches of law to trusts, as mentioned previously, it is nevertheless apparent that in some instances the facts of the matter would not provide a basis for awarding such a remedy. It is thus submitted that remedies be incorporated into the TPCA to protect third parties who contract with trusts.

It is further submitted that no valid reason exists as to why penalty provisions similar to those contained in legislation regulating other fiduciary functionaries cannot be included in the TPCA.[74] For example, section 102(1)(ii) of the Administration of Estates Act 66 of 1965 makes it an offence, liable on conviction to a fine or imprisonment for a period not exceeding twelve months, if an executor liquidates and distributes a deceased estate without letters of executorship. Section 144 of the Insolvency Act 24 of 1936[75] criminalises the failure of a trustee to, *inter alia*, submit an account to the Master or pay a sum of money to the Master by making such failure an offence, liable on conviction to a fine not exceeding R500. The following addition to the TPCA is thus, proposed:

> A trustee may not conduct the business of the trust with third parties recklessly, with gross negligence, with intent to defraud any person or for any fraudulent purpose. Non-compliance on the part of the trustee with this duty may result in personal liability being attributed to a trustee by the court, unless the court orders otherwise.[76]

6 Problematic provisions in the TPCA and recommendations

Currently, there are several provisions contained in the TPCA which, it is submitted, require amendment, either by including a penalty provision or by inserting a provision that regulates annual audits. The reasons for these proposed insertions are discussed under the relevant headings.

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73 See also B Wunsh "Trading and Business Trusts" (1986) *SALJ* 577-579 regarding s 424 of the 1973 Companies Act and s 64 of the Close Corporations Act 69 of 1984.

74 See also jurisdictions such as Bermuda and Singapore that have penalty provisions in their trusts statutes.

75 See also s 216 of the Companies Act which relates to a person who is convicted of an offence in terms of the Act.

76 Author's recommendation for the wording of an additional provision to the TPCA.

6.1 Section 6(1)

Section 6(1) of the TPCA provides:

> "Any person whose appointment as trustee in terms of a trust instrument, section 7 or a court order comes into force after the commencement of this Act, shall act in that capacity only if authorized thereto in writing by the Master."

By far, section 6(1) has generated the most case law and scholarly commentary. The most contentious issue regarding section 6(1) is the (in)validity of acts performed by unauthorised trustees. While a person becomes a trustee as soon as he accepts his appointment as such,[77] he cannot act in the capacity of trustee until he acquires the requisite authorisation from the Master which, in turn, is dependent on the furnishing of security.[78]

Prior to *Lupacchini v Minister of Safety and Security* ("*Lupacchini*")[79] the high courts had differing views on the effect of section 6(1) on a trustee's contractual capacity and capacity to litigate. There was thus a need for clarification by the SCA, which came about in *Lupacchini*. The case involved an unauthorised trustee's *locus standi* to institute legal proceedings. *In casu*, the court confirmed that the lack of a criminal sanction implied that the legislature intended for the acts of an unauthorised trustee to be invalid,[80] otherwise the prohibition would have no consequences at all.[81] Also, to interpret section 6(1) as nullifying only certain acts and not others would result in anomalies[82] and give rise to the very situation which the legislature intended to prevent.[83] While the judgment can be criticised, it goes beyond the scope of this article. The focal point here instead, is whether a penalty provision should be incorporated under the authorisation requirement if a trustee administers a trust without any form of authorisation. A trustee should not escape liability where there is non-compliance with the authorisation requirement. It is submitted that a trustee, like an executor who liquidates and distributes a deceased estate without letters of executorship, should be subject to a penalty provision. Thus, the proposed amendment should read:

> Any trustee who administers a trust estate without a letter of authorisation from the Master is guilty of an offence and will be liable on conviction to a fine or imprisonment not exceeding six months.[84]

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77 *Marais v Naude* 1987 3 SA 739 (A) 756F; Du Toit et al *Trust Law* 89.

78 Du Toit et al *Trust Law* 89.

79 *Lupacchini v Minister of Safety and Security* 2010 6 SA 457 (SCA).

80 465F-G.

81 466A-B.

82 466D-F.

83 468F-G. For criticism of *Lupacchini*, see MC Wood-Bodley "That 'Devilish Little Point' – The Impact of s 6(1) of the Trust Property Control Act 57 of 1988 on the Capacity of Trustees to Contract, Sue and Be Sued: *Lupacchini v Minister of Safety and Security*" (2011) *SALJ* 239.

84 Author's recommendation for the wording of an additional provision to the TPCA.

6.2 Section 20(3)

In terms of section 20(3), "[i]f a trustee authorized to act under section 6(1) is removed from his office or resigns, he shall without delay return his written authority to the Master".

Since a trustee's failure to comply with this duty could leave a trust incapacitated until his name is removed from the letter of authorisation, it is submitted that to ensure compliance with this duty, section 6(1) be amended to include a penalty provision. The Directive states that trustees must be informed that using old letters of authority will amount to fraud since they have been revoked. Other than that, the Directive states nothing further and does not specify any specific consequence if a trustee does not comply with section 20(3). The Directive also provides that if a trustee alleges that the letter of authority has been lost, an affidavit should be lodged by the trustee. No consequence is attached to not lodging the said affidavit either.

Thus, the proposed amendment to section 20(3) could read as follows:

> If a trustee who has been authorised to act under section 6(1) is removed from his/her office or resigns or loses his/her letters of authority, he/she shall return his/her written authority to the Master within thirty days from being removed or resigning from office or lodge an affidavit stating that said letter of authority has been lost within 30 days of becoming aware of said loss. Any person who fails to comply with this provision shall be guilty of an offence and liable on conviction to a fine or to imprisonment not exceeding three months.[85]

6.3 Section 11: Registration and identification of trust property

Section 11 provides:

> "Subject to the provisions of the Financial Institutions (Investment of Funds) Act, 1984 (Act 39 of 1984), section 40 of the Administration of Estates Act, 1965 (Act 66 of 1965), and the provisions of the trust instrument concerned, a trustee shall –
>
> *(a)* indicate clearly in his bookkeeping the property which he holds in his capacity as a trustee;
>
> *(b)* if applicable, register trust property or keep it registered in such manner as to make it clear from the registration that it is trust property;
>
> *(c)* make any account or investment at a financial institution identifiable as a trust account or trust investment;
>
> *(d)* in the case of trust property other than property referred to in paragraphs *(b)* or *(c)*, make such property identifiable as trust property in the best possible manner."

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[85] Author's recommendation for the wording of an additional provision to the TPCA.

This provision incorporates the common-law principle that trust property does not form part of a trustee's personal estate and, thus, that a trustee is under a duty to hold trust property in such a manner as to render it identifiable as trust property.[86] Compliance with this duty not only facilitates trust administration, but also allows a trustee to perform effectively his duty to account for trust administration.[87] Moreover, a trustee's actions relating to his bookkeeping, registration of trust property, investments and accounts must be conducted in such a manner that the assets of the trust are always identifiable as trust property.[88]

However, a trustee's non-compliance with this provision will not preclude the relevant property from falling outside the trustee's personal estate, provided that it can be identified as trust property in some or other way.[89] To assist in this regard, it is submitted that a statutory duty compelling trustees to submit trust accounts to annual audits be incorporated into the TPCA, with a failure to do so resulting in sanctions. Annual audits, it is submitted, will enable an auditor to identify whether a trustee indeed complies with this duty and will serve as a deterrent against trustees intermingling trust property with their personal property because of the consequent sanction that could ensue.

6.4 Section 12: Separation of trust property

Section 12 states that "[t]rust property shall not form part of the personal estate of the trustee except in so far as he as the trust beneficiary is entitled to the trust property".

Section 12 confirms the core element that a trustee holds two estates: that is, a private estate and the trust estate, as well as the principle that the trust is a segregated fund in that a trustee's private estate is separate from the trust estate.[90] In *Yarram Trading CC t/a Tijuana Spur v Absa Bank Ltd* it was noted that situations where a trustee combines trust property with his private property still require attention.[91] Again, a statutory duty to submit annual audits would assist for the reasons mentioned above.

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86 See *Yarram Trading CC t/a Tijuana Spur v Absa Bank Ltd* 2007 2 SA 570 (SCA) 576G; *YB v SB* 2016 1 SA 47 (WCC) 55D-E; Du Toit et al *Trust Law* 128.

87 Du Toit et al *Trust Law* 128.

88 *Olivier v Firstrand Bank Ltd* [2011] JOL 27019 (GNP) para 21. See also *Mahomed v Trustees of the Mohammedan* (2443/2007) [2008] ZANWHC 20 (3 July 2008) *SAFLII* <http://www.saflii.org/za/cases/ZANWHC/2008/20.html> (accessed 10-08-2020).

89 Du Toit et al *Trust Law* 129.

90 M de Waal "Is the DCFR Trust a 'Proper' Trust? An Evaluation from a South African Perspective" (2014) *Acta Juridica* 236.

91 *Yarram Trading CC t/a Tijuana Spur v Absa Bank Ltd* 2007 2 SA 570 (SCA) 576G-H.

The SALC recommended that provision be made to govern irregularities pertaining to trust administration.[92] To this end, section 15 of the TPCA provides:

> "If an irregularity in connection with the administration of a trust comes to the notice of a person who audits the accounts of a trust, such person shall, if in his opinion it is a material irregularity, report it in writing to the trustee, and if such irregularity is not rectified to the satisfaction of such person within one month as from the date upon which it was reported to the trustee, that person shall report it in writing to the Master".

The efficacy of this provision is questionable since the audits of trust accounts are not compulsory statutorily. It is doubtful that trustees who are involved in maladministration would make use of an auditor. Furthermore, copies of trust accounts need not be lodged with the Master's Office.

A statutory duty compelling trustees to submit trust accounts to annual audits, with a failure to do so resulting in sanctions, would, it is submitted, ensure that trustees studiously identify trust property as such, as they would have to provide details pertaining to the trust property for purposes of annual audits. An auditor would also be in a position to identify whether a trustee has indeed complied with this duty and thereby, the abuse of the trust form can be curbed. This statutory duty would, it is submitted, serve as a deterrent to trustees mixing trust property with private property.

While the costs of an audit may be an issue, it is submitted that section 30 of the Companies Act is instructive in this regard. Section 30(2)*(a)* requires the financial statements of a public company to be audited on an annual basis. Section 30(2)*(b)* relates to the financial statements of "any other company" and states *inter alia* that the financial statements must:

> "in the case of any other profit or non-profit company –
>
> (i) be audited, if so required by the regulations made in terms of subsection (7) taking into account whether it is desirable in the public interest, having regard to the economic or social significance of the company, as indicated by any relevant factors, including –
>
> *(aa)* its annual turnover;
>
> *(bb)* the size of its workforce; or
>
> *(cc)* the nature and extent of its activities".

Subsection (7) states that the Minister may make regulations that prescribe different requirements for different companies and prescribe *inter alia* which categories of private companies should have their financial statements audited as contemplated under section 30(2)*(b)*(i). It is submitted that a similar provision to section 30(2)*(b)* and (7) be included in the TPCA for the

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92 South African Law Commission *Review of the Law of Trusts* 63.

reasons mentioned above. The Minister may also provide for the penalties that may ensue in the event of a lack of compliance with this duty.

Considering the discussion of sections 11 and 12 of the TPCA, the following provision is proposed:

(1) A trustee shall ensure that the financial statements of the trust are audited on an annual basis, if so required by the regulations made in terms of subsection (2), taking into account whether it is desirable in the public interest, having regard to the economic or social significance of the trust, as indicated by–

(a) its annual value; and

(b) the nature and extent of its activities.

(2) The Minister may make regulations and prescribe different requirements for the trusts that shall have their financial statements audited as contemplated under subsection (1) as well as penalties that will ensue in the event of non-compliance.[93]

7 Conclusion

The SALC's reasons for rejecting the inclusion of penalty provisions are no longer justified. While many may argue that the inclusion of penalty provisions as well as a prohibition clause may deter persons from acting as trustees or endanger the flexibility of trusts, this argument does not justify the lack of such provisions in the Act. If anything, such provisions will ensure that trustees act in accordance with their duty of care and emphasise the importance of ensuring that there is compliance with their duties in general. It cannot be accepted that trustees can escape liability by relying on trite trust law principles. Furthermore, until it can be shown that there has been a reduction of persons willing to act in the capacity of executors, directors and trustees of insolvent estates because of penalty provisions, there appears to be no reason why such provisions should not be included in the Act governing an area of law where the abuse of the trust form has become as prevalent as it has. Opposition to the inclusion of compulsory audits may be based on the costs involved. However, the proposed amendment does not require that all trusts be audited. The annual turnover, nature and extent should serve as a guide in this regard. Compulsory audits may also bring into question the flexibility of the trust institution. However, audits will ensure that trustees comply with their duty to keep proper accounts and give effect to section 12 of the TPCA by ensuring that trust property is not intermingled with private property. While our courts have certainly tried to address the abuse of the trust form, it may be time for the legislature to step in and assist in this regard.

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93 Author's recommendation for the wording of an additional provision to the TPCA.