Going beyond the trust veil in insolvency and divorce matters

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ABSTRACT

Keywords: Trusts, control, intention, alter ego, sham, piercing, veil

This mini-dissertation is aimed at analysing the requirements the court takes into consideration when deciding to pierce a trust veil in either insolvency or divorce matters. A clear exposition of the legal nature of a trust is provided to determine how a trust affords the extensive protection to trust assets, the very characteristic that makes it as popular as it is today. It is due to this protection of trust assets that a trust has become the object of abuse by founders and trustees, and the court has felt it necessary to introduce a remedy.

In *Badenhorst v Badenhorst* the court stated that the company law doctrine of piercing the veil should be extended to trust law. Some authors criticised this judgement, and arguments pro(for) the extension is included in the conclusion. The research explored the circumstances that warrants the piercing of a trust veil and it was found that the court is likely to pierce a trust veil if the trust form was abused.

The study then shifts its focus to the type of abuse the court seeks to remedy. A trust can amount to be the alter ego of a person or a court can deem a trust to be a sham. The research investigates the distinction between the two in depth, and the resultant finding is that only alter ego trusts will be pierced by a court, since a sham trust means that no valid trust has in fact been formed and therefore there is no veil to pierce. Often the courts are confused by the two and the likelyhood of a trust being labelled a sham by South African courts are slim. To find that a trust was abused, the courts will look at the essential requirements of forming a trust to determine the validity.

The most important factors that the court considers when deciding to pierce the veil, is the type of control over the trust assets and the intention with which the trust is created or kept. An extensive analysis of the *Companies Act* and the doctrine of piercing the veil was done to probe their compatability with trust law and to see if the remedy is in fact effective and correctly applied. Case law to support the court's view and application of the mentioned doctrine is discussed and evaluated.

The study closes with an evaluation of the procedure of piercing the veil and the consequences following such piercing, as well as the arguments for allowing piercing of

a trust veil to force trust users to obey the basic trust idea of separation of enjoyment from control.

OPSOMMING

Sleutelwoorde: Trust, beheer, bedoeling, alter ego, sham, vertrouensluier

Hierdie mini-skripsie het ten doel om die vereistes wat die hof in aanmerking neem wanneer besluit word om die vertrouensluier te deurdring in gevalle van insolvensie of egskeiding te analiseer. ’n Duidelike uiteensetting van die regsaard van ’n trust word aangebied om te bepaal hoe ’n trust te werk gaan om die aansienlike beskerming aan trustbates te bied wat daarvan so ’n gewilde vorm maak. Dit is weens hierdie beskerming van trustbates wat trusts die onderwerpe van misbruik deur stigters en trustees geword het, en die hof het dit nodig geag om 'n remedie in te stel.

In *Badenhorst v Badenhorst* het die hof aangevoer dat die maatskappyreg se leerstelling van die deurdringing van die sluier uitgebrei behoort te word na trustreg. Sommige outeurs het hierdie uitspraak gekritiseer, en die argumente vir en teen so ’n uitbreiding word in die samevatting aangespreek. Die navorsing het die omstandighede wat die deurdringing van die vertrouensluier regverdig ondersoek en gevind dat die hof die vertrouensluier sal deurdring indien die trustvorm misbruik is.

Die fokus van die studie verskuif gevolglik na die tipe misbruik wat die hof wil remedie. ’n Trust kan neerkom op die alter ego van ’n persoon, of die hof kan die trust beskou as ’n voorwendsel. Die navorsing ondersoek die verskil tussen hierdie twee vorme van misbruik in diepte, en die gevolglike bevinding is dat slegs alter ego trusts deur die hof deurdring sal word, aangesien ’n voorwendsel-trust beteken dat geen geldige trust gevorm is nie en daar gevolglik geen sluier is om deur te dring nie. Howe word dikwels deur die twee verwar, en die waarskynlikheid dat ’n trust as voorwendsel afgemaak sal word in ’n Suid-Afrikaanse hof is baie klein. Die hof oorweeg die belangrikste vereistes vir die vorming van ’n trust om te kyk of die trustvorm misbruik is.

Die belangrikste faktore wat die hof sal ondersoek alvorens besluit word om die vertrouensluier te deurdring is die tipe beheer oor die trustbates en die bedoeling waarmee die trust geskep of gehou word. In-diepte analise van die Maatskappywet en die leerstelling van die deurdringing van die sluier is onderneem om die versoenbaarheid daarvan met trustreg te ondersoek en om te sien of die remedie korrek

en effektief toegepas word. Regspraak wat die hof se siening en toepassing van die genoemde leerstelling ondersteun word bespreek en geevalueer.

Die studie sluit af met ’n evaluasie van die prosedure om die sluier te deurdring en die gevolge van so ’n deurdringing, sowel as die argumente ten gunste van die deurdringing van die vertrouensluier om trust gebruikers te dwing om die basiese idee van die skeiding van genieting en beheer na te kom.

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LIST OF ABBREVIATIONS

AD	Appellate Division
CGT	Capital Gains Tax
CIR	Commissioner for Inland Revenue
INSOL	International Association of Restructuring, Insolvency and Bankruptcy Professionals
SA	South Africa
SALJ	South African Law Journal
SARS	South African Revenue Service
SCA	Supreme Court of Appeal
STELL LR	Stellenbosch Law Review
THRHR	Tydskrif vir Hedendaagse Romeins-Hollandse Reg
TSAR	Tydskrif vir Suid-Afrikaanse Reg

1 Context and methodology

1.1 Introduction and problem statement

The use of trusts in estate planning is not a new phenomenon, and people often transact with some form of a trust without realising it.[1] Although trusts are common in various jurisdictions, they mostly seem to exist in countries that are influenced by English law,[2] South Africa not being an exception.

In many instances where people are involved with trusts (through for example commercial transactions) they are unaware of the inner workings of such trusts, which might result in some uncertainties with reference too management, enjoyment[3] and control.[4] The reason could be that trusts today are part of the more modern South African law of trusts:[5]

> Currently the law of trusts is no longer confined to the traditional common law principles that used to exist.

Courts have, through their own interpretation, caused some development and have refined certain rules,[6] all of which had an influence on the creation and implementation of the *Trust Property Control Act*,[7] which is applicable to trusts. These developments are ever-evolving and trust law in South Africa has developed into a vibrant, challenging and well-respected area of law.[8]

The *Trust Act* was introduced in June 1988 and enacted in March 1989. This *Trust Act* is very brief and precise in its aim to regulate certain administrative elements of a trust,

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1 Vorster "When good intentions go bad" 245; Stafford *The dangers of translocating Company Law principles into Trust Law* 1.

2 Trusts were a creation of the English law of property and obligations, but also share a history with countries across the Commonwealth and the United States. See Honoré and Cameron *Honoré: The South African Law of Trusts* 21-27, Du Toit *South African Trust Law* 21-25 and *Estate Kemp v MacDonald's Trustee* 1915 AD 491, (*Estate Kemp*).

3 Enjoyment of trust assets can be defined as using and benefiting from trust assets. For example, a beneficiary who earns income from a trust, and even a founder, trustee and beneficiary can further benefit from the protection that a trust offers in the sense that assets are safe from claims and preserved for future family generations.

4 Stafford *The dangers of translocating Company Law principles into Trust Law* 1.

5 Vorster "When good intentions go bad" 245 and Van der Linde 2012 *THRHR* 386.

6 *Parker v Land and Agricultural Bank of SA* 2003 1 All SA 258 (T), (*Parker*). Cameron JA explained in *Parker* case that they are obliged to ensure the trust form is not abused and that they have the power and duty to develop the trust law by adapting the common law, legislation and *trust idea* into the principles of South African law of trusts. Van der Linde 2012 *THRHR* 372.

7 57 of 1988, (*the Trust Act*).

8 Vorster "When good intentions go bad" 245.

as well as to empower the Master of the High Court to supervise the activities of a trust.[9] Before the enactment of the *Trust Act*, trusts were regulated by way of common law, but since the enactment of the said act the law of trusts is no longer limited to the 'traditional common law principles'.[10]

Since the *Constitution*[11] was implemented over a decade ago, courts became obliged to protect beneficiaries[12] by giving effect to the duties of trustees as set out in the *Trust Act*.[13] Due to the limited scope of the initial *Trust Act*, the role of the judiciary has become more important, especially with reference to the interpretation of the *Trust Act*.

In several cases handed down by courts, the interpretation of the *Trust Act* is disputed. The respective courts apply the rules and legislation in accordance with their own interpretation of the available trust resources.[14] See for example *Badenhorst v Badenhorst*,[15] *Braun v Blann and Botha,*[16] *Commissioner for Inland Revenue v MacNeillie's Estate,*[17] *Estate Kemp,*[18] *Grobbelaar v Grobbelaar* unreported judgement[19] and *Jordaan v Jordaan*.[20] These judgements specifically deal with the protection of assets under the trust's veil/veneer and have lead to some significant developments in trust law, especially those heard by the Supreme Court of Appeal (SCA). It is important

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9 S1 and 3 of the *Trust Act* and Stafford *The dangers of translocating Company Law principles into Trust Law* 1.

10 Vorster "When good intentions go bad" 245 and Stafford *The dangers of translocating Company Law principles into Trust Law* 1.

11 *Constitution of the Republic of South Africa*, 1996, (Constitution).

12 The *Constitution* together with the *Trust Act* became important instruments for the courts, since the common law was no longer the only regulating authority for trusts. The *Trust Act* specifically empowers the Master of the High Court to regulate the actions of trustees, like acting in good faith. Van der Linde is of the opinion that *inter vivos* trusts are regulated by the law of contracts to some extent. He further notes that the law of contracts is built on a pillar of good faith. He states that the *Constitution* is based on fairness and equity and therefore courts and the legislator must develop rules that ensure that trustees comply with these standards. See Van Vuuren "When is a trust a sham?", Geach "Some Topical Issues relating to Trusts" and *Potgieter v Potgieter* 2012 1 SA 637 (SCA).

13 Vorster "When good intentions go bad" 245 and *Trust Act*.

14 In most cases the court approaches and applies available resources with regard to trust, each according to their own discretion and not rigidly. See for example *Parker v Land and Agricultural Bank of SA* 2003 1 All SA 258 (T), *Nedbank Limited v Thorpe* 2008 JDR 1237 (N) and *Peterson and Another v Claassen* 2006 5 SA 191 (C).

15 2006 2 SA 255 (SCA), (*Badenhorst*).

16 1984 2 SA 850 (A), (*Braun v Blann*).

17 1961 3 SA 833 (A), (*CIR v MacNellie's*).

18 1915 AD 491.

19 26600/98 (TPD), (*Grobbelaar*).

20 2001 3 SA 288 (C), (*Jordaan*).

to note that the terms *veil* and *veneer* is synonymous and used interchangeably by courts and academics. For the purpose of this research, veil will be used throughout.

A trust is a versatile entity that can be used (among other things) to safeguard a family's assets[21] and wealth against creditors, in business activities, to control wealth distribution to beneficiaries, to reduce potential estate duty and to minimise other tax liabilities.[22] Even though a trust provides this wide range of protection of trust assets, there are existing circumstances that warrant the removal of this protection. Recent case law such as *Badenhorst* and *Jordaan* support the notion that in certain instances, courts will go beyond the trust form and 'pierce'[23] the veil where a trust is abused. This holds true especially in instances where a trust is used to frustrate the claims of creditors or divorcing spouses. A trustee[24] who prevents or intentionally frustrates the claim of a divorcing spouse or a creditor (who would in the ordinary course of the law have a distribution claim for certain assets), by transferring his /her assets to a trust for safekeeping from claims under the protecting veil of a trust, could be attacked by the court in certain circumstances. This implies that the court can on request of the mentioned parties remove the protection that a trust provides for assets that the founder or trustee is attempting to keep out of reach of a divorcing spouse or creditors of the insolvent.

The aim with this research is to firstly analyse what the requirements are that the court takes into consideration when determining whether a trust veil will be pierced, and secondly, what the consequences are, if any, when the court decides to pierce the veil and expose the assets.

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21. There are many reasons for creating a trust-like asset protection, separating benefit from control, staying under the radar, in estate planning as an instrument to reduce estate duty and capital gains tax, to protect minors and for other tax reasons such as offshore trusts. This established protection mechanism confirms the purpose for establishing a trust.Vorster "When good intentions go bad" 246 and Geach "Some Topical Issues relating to Trusts".

22 See relevant case law such as *Parker*, *Nedbank Limited v Thorpe* 2008 JDR 1237 (N) and *Peterson and Another v Claassen* 2006 5 SA 191 (C).

23 Note that the term 'pierce(ing)' and 'lift(ing)' is synonomous and used interchangeably by courts and academics. The researcher refers to 'pierce(ing)' throughout the study. A term also often used by the courts is *to go behind the trust form* or *veil.*

24 It is important to know that it is not only the founder who can be accused of factually controlling (*de facto control*) the trust and its assets as his personal property. The founder could also be a trustee or beneficiary of that trust, where the trustee can be the one who physically controls the property for own benefit. Thus, for the purpose of this research, we will accept that the founder of the trust is also a trustee and whenever reference is made to a trustee who controls the trust and its assets, it is actually the estate owner (who exploits personal- and trust- assets all the same) that is referred to. See *Badenhorst*.

In order to succeed with a claim that trust assets should be deemed part of the estate owner's personal assets, evidence has to exist that a party controls the trust and were it not for the trust,[25] would have acquired and owned the assets in his own name.[26] Thus, one of the elements or requirements the court will consider when deciding to pierce the veil or not, is *control*. The type of control that a person has exercised over the trust assets will determine whether assets will be included or excluded for the purpose of redistribution of capital assets in terms of section 7(3) of the *Divorce Act.*[27] The concept of control in relation to a trust is often accompanied by the debate regarding **sham trusts** and the doctrine of the **alter ego**, which will be discussed in more detail in par 2.3 of this research.

A very important aspect in South African law of trusts that will be addressed in this research is *control*.[28] Control can take two forms. The first is *de facto* control, which denotes: "Existing in fact, whether legally recognized or not" and "exercising power or serving a function without being legally or officially established".[29]

Thus *de facto* control is actual control, which preferably should not be in the hands of the founder,[30] as opposed to *de iure* control, which is defined to mean "according to law".[31] *De iure* control is assigned to a person by law, usually the type of control that is allowed to trustees of a trust.

Apart from the control requirement,[32] other factors that will be considered and under scrutiny to determine whether this is a requirement the court might consider before piercing the trust veil, is the *intent* with which the founder created the trust. The intention of the founder to transfer the property to the trust or trustee must be clear from the onset of the contract between the two parties.[33] The purpose of a trust is undermined

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25 *Raath v Nel* 2012 5 SA 273 (SCA) par 13 and De Waal 2007 *Annual Survey* 849.
26 *Badenhorst* paras 9-12.
27 70 of 1979, (*Divorce Act*).
28 Stafford *The dangers of translocating Company Law principles into Trust Law* 1.
29 Farflex Date Unknown http://www.thefreedictionary.com/.
30 *De facto* control over a trust is often associated with alter ego trusts. See ch 2.3 for an in-depth discussion.
31 Farflex Date Unknown http://www.thefreedictionary.com/.
32 Control will be discussed in more detail in ch 2.3 of this research.
33 One of the essentials for creating a valid trust is that the founder must have the intention to create a trust and by this, creates and obligation, where the trustees must take control over the assets. To effect the validity, the founder must let go of his control over the assets he transferred to the trustees. Geach "Some Topical Issues relating to Trusts".

when the founder transfers assets to a trust, but intends to keep control of them. This intent with which the founder creates a trust, could be an indication of the type of trust he wishes to create. It is possible that the founder did not intend the trust to benefit a third, causing his trust to become attackable and the veil subject to piercing.

1.2 Research question

Based on the problem statement above, the main research question can be formulated as follows: Under which circumstances will a court go beyond the trust veil to make assets available for redistribution in insolvency and divorce matters? With the purpose of comprehensively addressing the primary research question, the following specific research questions are investigated:

(i) What is the legal nature of a trust instrument, and how does this nature contribute to the protection that trusts are said to have over assets within the trust?

(ii) What are the determining factors for courts when deciding whether trust is valid, and secondly, whether the courts can pierce the trust veil?

(iii) What is a sham/alter ego trust and how will these types of trusts allow for piercing of the veil?

(iv) Is the piercing of the veil doctrine available to courts in trust related matters?

(v) Given the factors in question three, what are the consequences for a trustee should these factors exist and the court decide to pierce the veil?

1.3 Method and structure

The adopted research methodology entails a qualitative approach by means of a literature review of relevant textbooks, law journals, legislation, case law and internet sources, relating to the nature and use of trusts. In broad terms, the most inclusive framework for the dissertation is case law. The aim is to establish the instances when the veil will be/has been pierced by explaining scenarios while making reference to case law. Both older and fairly recent cases are discussed.

This research is organised into six chapters. The following chapter focuses on the development of the general and legal nature and use of trusts. There are uncertainties regarding the exact requirements considered by the courts for piercing the veil. In order to grasp the scope of piercing a trust veil, the best point of departure is to refer to the original doctrine of 'piercing the corporate veil'. Thus, in the following chapter reference will be made to the company law where the doctrine originated.

Chapter three gives an account of the relevance of the *Companies Act* when it comes to piercing the trust veil. In addition, criticism on the introduction of the doctrine of piercing the corporate veil to trust law is also explored. This research reviews whether the principles relevant to piercing the corporate veil, borrowed from the *Companies Act,* can find application in trust law.[34] Although there are concerns about applying a company law doctrine to a trust law issue,[35] it could be argued that only the idea of the doctrine is taken from the Company law, but the doctrine will be developed and rewritten to be relevant and applicable to trusts.

Chapter four and five follows the same structure. The theory of the previous chapters is tested to case law to find how courts practically go about piercing the veil. A distinction is made between two matters concerning the abuse of trusts, namely insolvency and divorce.

One of the most recent cases involving claims by creditors that trust assets should form part of the estate owner's insolvent estate to settle his personal debt for the reason that he was controlling the same trust and assets as if it was his own, is the *Kaye* case.[36] In this type of insolvency matter, the estate owner who is declared insolvent, and who is also a trustee of a trust that conveniently contains assets that the insolvent donated to the trust, and the insolvent still benefits from this and aims to keep those assets in the trust away from the claims of personal creditors of the insolvent estate, is subject to scrutiny by court. Case law in chapter four will expose the practical application of 'piercing the trust veil' by courts.

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34 Stafford *The dangers of translocating Company Law principles into Trust Law* 125.
35 Stafford *The dangers of translocating Company Law principles into Trust Law* 125.
36 *Van Zyl v Kaye* 2014 4 SA 452 (WCC), (*Van Zyl v Kaye*).

The piercing of the trust veil is illustrated by looking at how this plays out in divorce matters.[37] The case of *Badenhorst*[38]*,* among others, is discussed. If a person uses and controls the trust in such a way that there is no distinction between enjoyment and control, the trust assets can be seen as the personal assets of the estate owner, and that person may no longer enjoy the protective veil of a trust instrument, and such assets may be taken into account when calculating the redistribution of wealth when a couple is divorcing. More detail about the legal nature of a trust will follow in chapter two, and case law relevant to divorcing spouses will follow in chapter five.

The concluding chapter seeks to offer recommendations based on judicial sources, as well as referring to other branches of law, like company law. It will also be discussed whether these sources have principles that are relevant and available in trust law circumstances. Finally the requirements for piercing the trust veil, if any, that are considered by the courts, are listed and discussed in brief to provide some legal certainty to trust founders, trustees, beneficiaries and prospective trust investors on the matter of trust protection and trust assets.

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37 See ch 4, *Parker v Land and Agricultural Bank of SA* 2003 1 All SA 258 (T) and *Nedbank Limited v Thorpe* 2008 JDR 1237 (N).

38 *Badenhorst* par 1.

2 Overview of the legal nature of a trust

2.1 Introduction

A critical aspect of this mini-dissertation is the nature of the trust,[39] especially with reference to protection of assets under the trust veil. A trust can be defined[40] as an arrangement[41], which can take the form of a contract or a will,[42] where ownership in property is by virtue of a trust instrument, made over or bequeathed[43] to a trustee(s) to be administered or disposed of in terms of the trust deed/instrument for either the benefit of the beneficiary(ies), or for the achievement of the object stated in the trust instrument/deed.[44] Strafford[45] notes that this definition is similar to the definition that was derived at the *Hague Convention*[46]*,* which states that:

> [T]he term "trust" refers to the legal relationship created *inter vivos* or on death, by a person, the founder, when assets have been placed under the control of a trustee for the benefit of a beneficiary or specified person.

The *Trust Act* adopted the definition as it was accepted at the *Hague Convention*[47] and states that assets in the trust constitute a separate estate and is not part of the trustee's

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39 Vorster in *Misbruik as gevolg van die miskenning van die besigheidstrust* states that academics often confuse readers when classifying trusts, each writer according to their own understanding and liking 20. Some of these examples are seen in Honoré and Cameron *Trusts* 14-17. According to Vorster, Olivier's approach to classification is the best in terms of accuracy, the reason being that his classification considers the theories of all the other writers as well. Olivier identifies four aspects that would classify a trust, its nature and management. In short, they are the way the trust originated, secondly, the discretion that a trustee has, in whom the rights over the assets vests and the reason/aim of creating the trust. (Olivier and Strydom *Trust law and Practise* 1). All of these aspects are addressed in this research.

40 The term *trust* is conventionally used in both the wide and narrow sense. See further du Toit *South African Trust Law* 2.

41 Geach "Some Topical Issues relating to Trusts".

42 Any agreement that is legally binding.

43 Transferred by means of made-over or bequeathed. A trust *mortis causa* is created by way of a will: Du Toit *South African Trust Law 108.*

44 Geach "Trusts: Are they still relevant and useful?" 143.

45 Vorster "When good intentions go bad" 246 and Stafford *The dangers of translocating Company Law principles into Trust Law* 10.

46 *Convention on the Law Applicable to Trusts and on their Recognition* (1985) A3, (*Convention*)

47 A3:
For the purposes of this Convention, the term "trust" refers to the legal relationships created *inter vivos* or on death by a person, the settlor, when assets have been placed under the control of a trustee for the benefit of a beneficiary or for a specified purpose.
A trust has the following characteristics –
a) the assets constitute a separate fund and are not a part of the trustee's own estate;
b) title to the trust assets stands in the name of the trustee or in the name of another person on behalf of the trustee;
c) the trustee has the power and the duty, in respect of which he is accountable, to manage, employ or dispose of the assets in accordance with the terms of the trust and the special duties imposed upon him by law.

own estate.[48] The definition of a trust and the included separation of the trust assets from the trustee's estate,[49] is a trust in the narrow sense.[50] Distinguishing between the two types of trusts is not always easy, because the most insignificant detail is relevant to determine the type of trust. According to du Toit[51] the most noticeable difference is:

> The distinction between trusts in the wide and narrow sense becomes pertinent when trusteeship under each is at issue. The trustee of a trust in the narrow sense holds an office and is, as such, subject to control by the Master of the High Court and the High Court itself. Whereas trustees in the wide sense do hold office...others do not necessarily act in an official capacity.

Just to clarify, in the narrow sense (like most discretionary family trusts)[52], "trust" refers to the trust as a legal institution.[53] A trust in the narrow sense has similar characteristics to trusts in the wide sense;[54] for example, the core idea that separation of ownership and control from the enjoyment of the trust benefits, are derived from trusts in the wide sense. Trusts in the narrow sense are defined by Cameron in *Honoré's*[55] as being:

> [A] legal institution in which a person, the trustee, subject to public supervision, holds or administers property separately from his or her own, for the benefit of another person or persons or for the furtherance of a charitable or other purpose.

On the other hand, trusts in the wide sense are described by Olivier[56] as: "A relationship of confidence or good faith with respect to property and beneficiaries". This relationship could arise in the case of a trustee of an insolvent estate or the curator of a mentally ill person.[57] This type is rarely referred to as a trust.[58] It is, however, important to bear in mind that in the wide sense, the trustees never become the owners of the property, they

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The reservation by the settlor of certain rights and powers, and the fact that the trustee may himself have rights as a beneficiary, are not necessarily inconsistent with the existence of a trust.

48 Trust assets can therefore not be used in the settlement of claims against the estates of the founder or trustees (A3 of the *Convention* and Vorster "When good intentions go bad" 246).

49 S12 of the *Trust Act* states that property in a trust is separate from the personal estate of the trustee.

50 Smith *The Authorisation of Trustees* 6.

51 Du Toit *South African Trust Law* 108.

52 The control normally vests in the trustees, depending on the reservations made by the founder. Some business trusts are also categorised under this heading, and is falling short of keeping control and enjoyment of trust assets separate. Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html

53 Honoré and Cameron *et al South African Law of Trusts* 343,344.

54 Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 18. Some features like the separation of enjoyment from control, which characterises a trust in the wide sense, is also an element of a trust in the narrow sense. Honoré and Cameron *South African Law of Trusts* 343,344 and Stafford *The dangers of translocating Company Law principles into Trust Law* 9.

55 Honoré and Cameron *South African Law of Trusts* 343,344.

56 Olivier and Strydom *Trust Law and Practice Set* 548.

57 Smith *The Authorisation of Trustees* 4.

58 Smith *The Authorisation of Trustees* 4.

merely hold the property for the benefit of a beneficiary in an official capacity as trustees.

However, it is not common for South African courts to make this distinction. This chapter discusses the legal nature, use and forms of trusts. Further reference will be made to the control requirement and the concept of a trust as a person's **alter ego**.

2.2 Legal nature of a trust

2.2.1 Introduction

One of the primary reasons why estate owners make use of a trust as part of their estate planning is to safeguard assets and wealth against risk in addition to a variety of other reasons.[59] In the *Parker* case,[60] the SCA observed that:

> [T]he great virtue of the trust form is its flexibility, and the great advantage of trusts, their relative lack of formality in creation and operation. The trust is an all-purpose institution, more flexible and wide-ranging than any of the others.

Regardless of what the reason for creating a trust is, the simplicity in creating a trust contributes to the attractiveness of this tool and to add to this attractiveness, there are different types of trusts that a founder can engage in[61] to serve his needs best.

De Waal[62] admittedly notes in his contributions that questions regarding the exact legal nature of a trust institution are a familiar sight and a subject that often emerges in academic records. It is important to understand the legal nature of a trust for more than one reason. First, to ensure that prospective and *bona fide* trust users know how to engage with this entity. This prevents their trusts from being placed under scrutiny by the courts and even possible piercing of the veil, exposing the assets to claimants. Second, the nature of a trust is what protects the assets in the trust,[63] and if a person is uninformed about the extent to which the protective veil will endure, such a person can be surprised when the trust veil has to be pierced. While any property can be

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59 Other reasons like reduced estate duty and CGT, protection of minors, tax reasons like offshore investments and for separation of benefit from control. Vorster "When good intentions go bad" 245, Edmonds Date Unknown http://www.edmondsjudd.co.nz/dms/images/custom_content/Fineprint_45_may.pdf.

60 *Parker* case par 273D.

61 Vorster "When good intentions go bad" 246 and Stander 2008 *INSOL.* 165.

62 De Waal 2007 *Annual Survey* 848.

63 Vorster "When good intentions go bad" 246.

transferred to a trust, persons generally transfer assets that increase in value.[64] The motivation behind this could be that when a founder transfers his property to a trust, a trust pegs the growth of assets in the estate of the founder, relieving the estate from assets increasing in value, which indirectly reduces estate duty and capital gains tax in a person's own estate. Another reason could be that the trust instrument provides protection under a veil,[65] preventing creditors or even divorcing spouses to make claims in terms of the trust assets. Consequently, the measure of protection that the trust can afford to trust assets is especially helpful where trustees are in a position where their personal estates become either insolvent or subject to redistribution claims as a result of a divorce.

2.2.2 The trust as an independent entity or legal person

The point of departure for this topic is to determine who the owner, the founder and trustees are, and who will be in control of the trust assets. In each of the *Badenhorst, Parker* and *Thorpe*[66] cases, the court stated: "This trust, however, remained an independent entity", a separate entity, one that is an accumulation of assets and liabilities.[67] Strictly speaking it is incorrect to refer to a trust as a 'separate legal entity', as was confirmed in *CIR v MacNellies*[68]:

> Neither our authorities nor our Courts have regarded it as a *persona* or entity. It is trite law that the assets and liabilities in a trust vest in the trustee.

According to the *Annual Survey*[69] the theoretical point of departure is that a trust is not a legal person, but that the trust estate is an accumulation of assets and liabilities, and does form a 'separate entity' in the sense that a trust's estate is kept separate from a founder/trustee's estate.[70] This was reconfirmed in *Raath v Nel*[71]. Although a trust is not seen as a legal person, in some situations, legal status is conferred onto a trust. The

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64 Any type of residential property, farms and agricultural property. See Geach "Trusts: Are they still relevant and useful?" 143.

65 This established protection mechanism confirms the purpose for establishing a trust. See Vorster "When good intentions go bad" 246.

66 *Thorpe v Trittenwein* 2007 (2) SA 172 (SCA), (the *Thorpe* case).

67 De Waal 2007 *Annual Survey* 848. Also see recent judgements *Badenhorst* par 855A, *Parker* par 258A and *Thorpe* par 9.

68 Paras 840G-H.

69 De Waal 2007 *Annual Survey* 848.

70 *Badenhorst* par 855A, *Parker* par 258A and *Thorpe* par 9.

71 *Raath v Nel* 2012 (5) SA 273 (SCA) par 13, (*Raath v Nel*). See also *Parker* and *Niewoudt v Vrystaat Mielies Edms Bpk* 2004 3 SA 486 (SCA).

situations where this might be the case are briefly discussed here. The *Income Act*[72] was one of the first provisions to be influenced by trusts and to in turn influence trusts. In *CIR v Friedman*[73] the court ruled that a trust cannot be seen as a legal person in terms of section 5 of the *Income Tax Act*. The result of this was that trusts are not liable for any taxes under the mentioned act. This was not the intention of the legislature, and as a result this act was amended to include a trust as a legal person.

Other provisions that include a trust as a legal person is the *Insolvency Act*,[74] the new *Companies Act*, the *Firearms Control Act,* the *National Credit Act* and the *Deeds Registries Act.*[75]

The fact that these provisions refer to a trust as a juristic person does not confer this status to trusts in general, but only to the extent that a trust crosses paths with one of the mentioned provisions.[76] For example, income generated by a trust will give effect to the applicability of the income tax act etc.

2.2.3 Separation of estates

In *CIR v Friedman* it was again confirmed that a trust is not a legal person, but can be viewed as an accumulation of rights and duties that form the trust estate. As such it is regarded as a separate entity from the founder's personal estate.[77] After the transfer of assets to the trust, the trustees will retain the assets and become the new legal owners of those assets in their capacity as trustees, regardless of any previous legal relationship that they had with the property before.[78]

It is this legal veil that forms a shield for the protection of the trust assets. The veil of a trust is the characteristic responsible for the trust's ability to protect the property

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72 58 of 1962, (*Income Tax Act)*.

73 *CIR v Friedman* 1993 1 SA 353 (A) par 358F, (*Friedman*).

74 In *Magnum Financial Holdings v Summerly* 1984 1 SA 160 (W) par 163, a trust was seen as a debtor (same as a natural person) and is therefore sequestrated and not liquidated like a body corporate.

75 47 of 1937. In the case of *Mkangeli v Joubert* 2002 4 SA 36 (SCA), following the case of *Joubert v Van Rensburg* 2001 1 SA 753 (W), *the Deeds Registries Act* was amended and inserted in s102, trusts, in the definition of a person.

76 Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html.

77 *Parker* par 855C and Vorster "When good intentions go bad" 246.

78 Even though the assets belong to the trust, the trustees become the owners of the assets and they are registered in the name of the trustees in their official capacity as trustees of the trust in issue. Control over the mentioned assets also vests in the trustee. See also the *Parker* case where Cameron JA states: "the trustee is appointed and accepts office to exercise fiduciary responsibility over property on behalf of and in the interests of another" par 262B.

specifically transferred to it.[79] The trust veil refers to legal separation of ownership between the personal estate of the founder/trustee and the transferred property in the trust.[80]

In the recent case of *Raath v Nel*, Majiedt JA once again sounded a warning regarding the 'separateness' of the trust estate. Majiedt contends that this 'separateness' might encourage the abuse of a trust form.[81]

The abuse of the trust form leads to circumstances that may warrant a court to go beyond/pierce the trust veil.[82] The increase in abuse can be ascribed to the evolution of a "newer type of trust" in South Africa.[83] The main characteristic of this *newer* type of trust is the founder and trustees' retention of control or enjoyment of the trust assets. They can make use of the trust property as if it is still part of their personal property.[84] This "newer type of trust" (mostly family businesses/trusts) is born when a person creates a trust for either estate planning purposes or to avoid restrictions involved in creating a company for example, but everything else remains as before the trust was created.[85]

In *Braun v Blann* the same issue was considered and the court noted that "[I]n its strictly technical sense the trust is a legal institution *sui generis*".[86] In other words, *prima facie* a trust depicts a legal entity such as a company, except for one important characteristic, namely that a trust lacks *locus standi* (legal standing). A trust can therefore not be sued

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79 Vorster "When good intentions go bad" 246.

80 Stafford *The dangers of translocating Company Law principles into Trust Law* 20.

81 De Waal 2007 *Annual Survey* 848, *Raath v Nel* paras 13-14 and *Parker* par 855C.

82 Harding *Importance of adhering to the basic trust idea* 4.

83 See ch 2.3 for a detailed discussion. Further see Stander 2008 *INSOL* 156 and Harding *Importance of adhering to the basic trust idea* 5.

84 This characteristic is similar to the alter ego doctrine found in foreign law, see ch 2.3 of this research and Harding *Importance of adhering to the basic trust idea* 5.

85 Harding *Importance of adhering to the basic trust idea* 5, *Parker and Niewoudt v Vrystaat Mielies (Edms) BPK* 2004 3 SA 486 (SCA) par 493E.

86 Paras 859E-H.

because it is not a person and cannot be cited as such.[87] However, the trustees of the trust can be sued in their capacity as trustees.[88]

2.2.4 Trusts v fideicommissaries

Apart from all the debates on the legal nature of a trust, scholars argue that a trust could resemble a *fideicommissum* depending on the type of trust. The two cases most influential in developments surrounding testamentary trusts are the *Estate Kemp* case and the *Braun v Blann* case.

In these cases, a trust was equated with a fiduciary, whereas a trustee was associated with a *fideicommissum*:[89]

> However, a problem arose in the sense that the *fideicommissum* did not recognise simultaneous vesting of rights in both the fiduciary and the *fideicommissary*, as, for the *fideicommissary*, *dies cedit* generally only occurred upon the fulfilment of a specified condition. Therefore the challenge was to find a way in which vesting could take place in the *fideicommissary* "in spite of the *fideicommissary* nature of the bequest".

Regardless of whether the testamentary trust was associated with a *fiddeicommissum*, which was sternly criticised, the *Estate Kemp* case contributed significantly to the development of the South African trust law. The result was that it was established that the trustee becomes the owner of the trust property and the beneficiary obtains a personal right against the trustee for the assets bequeathed to him. In *Estate Kemp*,[90] Innes CJ acknowledged the testamentary trust[91] as a form of trust in SA. In this regard Olivier[92] states that:

> Although it may be tempting to equate the trust idea with the *fideicommissum* of Roman law, such a comparison is no more than an intellectual exercise. The origin and development of the trust in English law has no connection with Roman law and efforts to try to establish a link between the two institutions are futile.

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87 A trust can never be regarded as being a person. There are few exceptions where a trust is regarded as being a person by statute: *Income Tax Act* 58 of 1962, *Value Added Tax Act* 89 of 1991, *Deeds Registries Act* 47 of 1927 and *Companies Act* 71 of 2008.

88 Stander 2008 *INSOL* 165-166 and See also the *Parker* case where Cameron JA states: "the trustee is appointed and accepts office to exercise fiduciary responsibility over property on behalf of and in the interests of another" par 262F.

89 Smith *The Authorisation of Trustees* 23, Stafford *The dangers of translocating Company Law principles into Trust Law* 21 and *Estate Kemp* paras 500-501.

90 Paras 499-501,861 and 864 and Olivier *Trust Law and Practice* 18.

91 See also Smith *The Authorisation of Trustees* 9, Corbett *THRHR* 264, De Waal *SALJ* 555 and De Waal *SLR* 76.

92 Olivier *Trust Law and Practice* 8.

The second important case, namely *Braun v Blann,* followed *Estate Kemp* and the goal to equate a testamentary trust with a *fideicommissum* was rejected by the appellate division.

Olivier's opinion[93] discussed above appears to support Joubert JA's judgement in *Braun v Blann*[94]. Moreover, Joubert JA's *dictum* that "historically and jurisprudentially the *fideicommissum* and the trust are separate and distinct legal institutions",[95] makes it clear that the two are, at the very most, only comparable in theory.[96] In *Braun v Blann* the following important finding was reached:[97]

> The trust could not be equated with the *fideicommissum*. The Court stated that to equate the trust with the *fideicommissum* was both historically and jurisprudentially incorrect as they were separate legal institutions.

In spite of the legal debate concerning testamentary trusts and *fideicommissums*, it was essential to create a common legal understanding of this type of trust and the nature of a *fideicommissum* to clear the air of the troublesome and inconvenient issues surrounding it.[98] The court subsequently concluded by saying that a testamentary trust is a legal institution *sui generis*.[99] Therefore, a trust and a *fideicommissum* are for all purposes quite different and separate. After many instances of equating the testamentary trust with a *fideicommissum*, [100] it was finally decided by the appellate division that the *inter vivos* trust is created with the aim of benefitting a third party. The stipulation of benefitting a third party in terms of a contract is referred to as a *stipulatio alteri*,[101] and the court wrongly equated the *fideicommissum* with a testamentary trust.[102] Thus, both the testamentary trust and the *inter vivos* trust were found to be an institution *sui generis*,[103] and it is therefore correct to refer to a testamentary trust as a *stipulatio*

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93 Olivier *Trust Law and Practice* 8.
94 Paras 858 (H) –866 (D).
95 Par 859 (C).
96 The position regarding the comparison between a trust and a *fideicommissum* was first heard and judged in *Estate Kemp* and was later changed to the current legal position as in *Braun v Blann*.
97 Par 859 (C) and 866 (B).
98 Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html.
99 Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 23,*Badenhorst* and Du Toit *SA Trust Law* 167-169, De Waal 2001 *Stell Law Review* 82 and *Honoré* and Cameron *Trusts* 56.
100 See *Braun v Blann* par 859E.
101 Refer to ch 2.2.5.2 for detail, *Crooks v Watson* 1956 1 SA 277 (A) and was reconfirmed in *Hofer v Kevitt* 1998 1 SA 382 (SCA).
102 *Braun v Blann* par 859E.
103 Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html, *Badenhorst* par 8 and *Braun v Blann* par 859E-H.

alteri rather than a *fideicommissum*[104]*.* The reason for this is that in both instances a trustee and determinable beneficiaries are appointed, and the trustees are given the power to manage the trust for the benefit of the beneficiaries.

There is, however, a variety of trusts available, depending on the aim of such a trust.[105] The different types of trusts will be discussed briefly below.

2.2.5 Different types of trusts

2.2.5.1 The *mortis causa* or testamentary trust

Testamentary trusts eventuate when a person states in his last will/testament that a trust should come into being upon his death.[106] The founder's will/testament then operates as the trust deed spelling out the terms of the trust.[107] The deed will identify the beneficiaries and state under what circumstances beneficiaries are to benefit and when the trust is to terminate. There are various reasons and circumstances to consider when deciding whether to create a testamentary trust, some relating to family issues like minor children or a surviving spouse in need of maintenance, disability provision (special trusts) and monetary and tax considerations.[108] When it comes to minor children and tax, an estate planner may suggest that the estate owner creates a testamentary trust for maintenance, either for the minors or the surviving spouse. This reduces the estate owner's dutiable estate and reduces the capital gains tax payable.

There are both advantages and disadvantages to a testamentary trust. Because a testamentary trust is created upon the death of the 'founder', it tends to be driven more by the needs of the beneficiaries (i.e. minors) than by tax considerations. In contrast, living trusts, which are created during the founder's lifetime, tend to be driven more by tax considerations.

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104 Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 22 and *Braun v Blann* 866H-867A and 859F-G.

105 Vorster "When good intentions go bad" 246.

106 *Estate Kemp*.

107 Olivier *Trust Law and Practice* 25-26.

108 Schoeman 2009 http://www.findanattorney.co.za.

It is still not clear whether the testamentary trust is regulated by the trust law or by the law of succession, especially when it comes to the rules of interpretation and the amendment of the trust document.[109]

2.2.5.2 *Inter vivos* trust[110]

An *inter vivos* trust[111] can be defined as a binding contract between two or more parties[112] while they are alive,[113] usually the founder and a trustee(s), for the benefit of a third party. More specifically, in the case of *Crookes v Watson*,[114] the Supreme Court of Appeal stated that it is a contract similar to a *stipilatio alteri*, which is a contract for the benefit of a third party (i.e. the beneficiaries).[115] For example, a father and mother may create a trust for their children so that the children can survive off the trust should the parents die before the children are independent. In this case the third party need not be the children, it can also be a surviving spouse or even the appointed guardians of the minors who will be financially maintained from the trust money. This mini-dissertation is limited to instances associated with *inter vivos* trusts.

The next form of a trust, the bewind trust, is a trust that is structured in either of the two ways mentioned above, but it has an element of vesting added to it. Thus, a bewind trust can be an *inter vivos* or testamentary trust, but the rights of the beneficiaries have already been vested in them. An interesting aspect regarding bewind trusts constitutes the reason for limiting the focus to *inter vivos* trusts.

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109 Smith *The Authorisation of Trustees* 24 and Olivier and Strydom *Trust Law and Practice* 20, 38.

110 An *inter-vivos* is defined in the *Trust Act* as a trust other than a testamentary trust.

111 As was indicated supra at 5.2, the *inter vivos* trust is now also described as an institution *sui generis* in the *Badenhorst* case.

112 *CIR v Estate Crewe* 1943 AD 656 and Vorster "When good intentions go bad" 247.

113 Smith *The Authorisation of Trustees* 8.

114 *Crookes v Watson* 1956 1 SA 277 (A). Also see Olivier 1997 *TSAR* 766, Pace and Van der Westhuizen *Wills and Trusts* 33 and 36 and Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 24.

115 An *inter vivos* trust is based on the law of contracts and more specifically as a contract for the benefit of a third party. See also Vorster "When good intentions go bad" 246.

2.2.5.3 Bewind trust[116]

The term comes from Dutch law (bewind) and Roman-Dutch law (*bewindhebber*).[117]In a bewind trust, the founder makes a gift or bequest to the beneficiary and vests the administration of the assets in the administrator or trustee. With this kind of trust, the trust beneficiaries acquire ownership of the assets,[118] with the trustee having only administrative control over these assets.[119] This type of trust is grouped under the narrow definition of a trust.[120]

2.2.6 Conclusion

There is no doubt that the exact nature of a trust is not cast in stone and remains a debated topic in our law. The aim of the section above was to answer the question of what the legal nature of a trust instrument is and how this nature contributes to the protection that trusts are said to offer assets within the trust.

The discussion established that a trust exists as a separate entity, and the estates of the founder, trustees and beneficiaries are kept separate from the estate of the trust. Even though a trust enjoys independent standing, it generally has no legal personality under the common law:[121]

> Although the common law does not recognise the trust as a legal person, the trustee in his official capacity is, for several purposes, regarded as a separate entity.

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116 A bewind trust is not entertained to purport either the sham or alter ego trust. The reason is that in a bewind trust, the assets vests in the beneficiaries of the trust, resulting in the beneficiaries' being the legal owners thereof. The sham and alter ego discussion in ch 2.3 will show that the trustees differentiate between their personal and the trust estates. The discussion on this separation cannot be explained by the use of a bewind trust due to the vesting that already took place, the assets are already that of the beneficiary and may do with it as they please. *Inter vivos* trusts will therefore the main object of discussion.

117 *Braun v Blann*.

118 De Waal and Schoeman-Malan *Succession* 159. If the structure corresponds with that of the bewind, where contributing beneficiaries are involved, as is the case in certain business trusts, the ownership of the trust property is vested in the beneficiaries.

119 See *Braun v Blann*, Stafford *The dangers of translocating Company Law principles into Trust Law* 23 and Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html.

120 Smith *The Authorisation of Trustees* 7, Stafford *The dangers of translocating Company Law principles into Trust Law* 23 and Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html.

121 Vorster defines legal personality as being: "die vermoë om in die regsverkeer te kan deelneem, eie regte en verpligtinge te hê, in die posisie te wees om bates te verkry, 'n party tot 'n kontrak te wees, 'n eis te kan instel en om in die hof gedagvaar te kan word." See Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 8.

There are certain instances where a trust is deemed to have legal personality and where it falls within the definition of a juristic person. The instances in which a trust is seen to have legal personality are delineated in several legislative provisions such as the *Income Tax Act* and the *Companies Act*.[122] In agreement with Honoré [123] it can be concluded that a trust is not a legal person, but in some instances can be referenced as a juristic person *sui generis*.

The next paragraph introduces and discusses what is commonly referred to as the *newer type of trust* or the *business/family trusts*. The protective mechanism (veil) that a trust offers to the trust assets provides protection against risks and claims and is often abused by trustees. Exploitation of the trust figure occurs when trustees want to benefit from the extensive protection that a trust veil provides, yet they do not want to obey the general or statutory requirements of a valid trust. The exploitation can be seen in a vast number of recent cases dealing with the issue.

2.3 Newer type of trust

The court noted in *Braun v Blann*[124] that the South African law of trusts has gone through an era of evolution. In every aspect of the law, no one thing is set in stone, and the law constantly develops to form new legal positions and possibilities that people can explore. Thus, it is not surprising that this newer type of trust, unknown to trusts in general,[125] has been introduced into our system and has moved under the radar for a while. With this type of trust[126], it is not the trust that is abused *per se*, this type of trust rather came into existence as a result of the abuse of a normal trust. Harmse JA recognised the rise of a *new type of trust*[127] and describes it as follows:[128]

> The trust deed in this case is typical of a newer type of trust where someone, probably for estate planning purposes or to escape the constraints imposed by corporate law, forms a trust *while everything else remains as before*. Mr Nieuwoudt, the first appellant, was the trust donor. They are the only income beneficiaries. Only he can appoint

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122 See par 2.2.2 of this mini-dissertation.

123 Honoré and Cameron *Trusts* 72, Pace and van der Westhuizen *Wills and Trusts* 18, Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 12 and *Harris v Rees*.

124 Paras 859 E-G and Harding *Importance of adhering to the basic trust idea* 12.

125 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) par 493E.

126 Hereafter the *newer type of trust* can be referred to as a *business or family trust*.

127 Within the context of this decision, the court refers to the so-called birth of the *business trust,* which is still an *inter-vivos* trust. However, this trust lack to conform to the general trust rules in terms of separation of estates and control.

128 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) par 493E.

> further trustees. The trust may conduct business, in particular that of farming. One wonders how the farming operations are conducted given the fact that the trustees have to act jointly. (Own emphasis added)

The emphasis is placed on the fact that even though founders create trusts in the normal way, they do not create it for the benefit of a third party, but rather for their own benefit. Vorster[129] mentions that the main objective of business trusts are to use the trust assets for business activities and to generate income and make a profit from them in this way. Some founders who create family or business trusts do so merely so that it can "serve as a type of veneer"[130] behind which they can continue to control their assets the way they use to, enjoying trust protection of their assets as if the trust was never created.[131] The failure to separate the trust estate from that of the founder is often referred to as the debasement of the core idea of a trust.[132]

Complying with the basic trust idea is often easier said than done.[133] Many trusts are merely an extension of the founder's personal estate. Whether founders have this intention from the outset when creating a trust or if they develop the intention at a later stage depends on the circumstances. This intentional factor can determine whether a sham trust has been created or whether the trust form has merely been abused to serve as an **alter ego** of a person. This is one of the matters that the court will consider when deciding whether to pierce the trust veil or not, and will be discussed in more detail in chapter 2.4. The rise of this type of trust has resulted in a number of scholarly writings and court cases. The doctrine of piercing the veil is becoming a frequent theme in cases relating to trusts and therefore it is important to establish the exact requirements, if any, that the courts consider before applying the doctrine to a case. If these requirements can be determined, some legal certainty might be restored to trusts users. The doctrine serves to protect third parties, creditors and spouses. Chapters 4 and 5 deal with case law in this regard in more detail.[134]

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129 Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 1 and 37-64.

130 Harding *Importance of adhering to the basic trust idea* 12.

131 *Nieuwoudt v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) par 493E and Harding *Importance of adhering to the basic trust idea* 12.

132 Van der Linde 2012 *THRHR* 372 and *Van der Merwe NO v Hydraberg Hydraulics CC and Others*, *Van der Merwe NO and Others v Bosman and Others* 2010 5 SA 555 (WC) par 87,(the *Van der Merwe* case).

133 Harding *Importance of adhering to the basic trust idea* 20.

134 *Jordaan* case.

The discussion so far reveals that trust forms, both in general and the newer type, are often abused and that protection has to be provided to innocent creditors and divorcing spouses who have claims against trust assets if courts find that abuse is present. The paragraphs below delineate the elements used to determine whether a trust has been abused and constitutes either a sham- or alter ego-trust, and whether these elements are the requirements used by courts to determine if the doctrine of piercing the veil is relevant, will be researched.

2.4 Intention of parties to a trust agreement

Certain requirements have to be met to create a valid trust[135]. It must be clear that:[136]

(a) the founder had the intention to create a trust and what the intention was when creating a trust,

(b) the property is certain; and

(c) the beneficiaries must be clearly identifiable.

If one of these requirements is absent, a trust will not come into existence and it might be deemed a sham. A formal and written trust agreement/deed is the preferred way to record the objectives of the trust, because it can serve as proof of the intention of the founder, as well as the presence of the two remaining requirements. This proof is necessary to determine whether the trust created is valid or not. If a valid trust has been created, a different consequence related to trust assets will follow than would be the case where a sham has been created. This consequence will be discussed at the end of this chapter.

In the case where the founder/drafter of a trust drafts a deed, but fails to expressly note in the agreement the true intention with creating a trust, the ulterior motives of the founder to create a sham or alter ego trust might become apparent.[137] Recording of the intention will eventually assist with identifying a sham trust. Where the trust situation in

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135 Can be concluded in a formal or an informal manner by means of written documentation.
136 Manulife Financial 2014 http://www.manulife.com.
137 Kessler 1999 *OTPR* 138.

reality differs significantly from the intention mentioned in the trust deed, the possibility exists that the trust may be a sham or an alter ego.[138]

It is in the interest of trusts and the users of trust that trust security is not undermined.[139] Where a trust is set up for the protection of a beneficiary and to safeguard family assets for future beneficiaries, it is important to adhere to general trust requirements to secure the protective veil over the assets. This can be done by making the intention of the founder clear in the deed. If the intention requirement is lacking or not adhered to, then the trust security/veil will not extend over the assets as it is supposed to,[140] therefore not protecting the beneficiary and trustees. This situation can be avoided by reflecting the true intention of the founder in the deed. Whether the intention was to ensure financial protection for a minor beneficiary, to protect a beneficiary against claimants or to safeguard family assets, the motivation must be clearly stated and it must be ensured that this intention does not change along the way.[141] Grant submits that:[142]

> [i]f a trust is to survive claims that it is the alter-ego of a trustee/beneficiary/[settlor] or a sham, it should in substance fulfil the necessary requirements of a trust. This means that it should not be worded in such a way that the settlor has the power to ensure that the assets can be utilised by him/her as a beneficiary in ways which he/she prefers. This means that powers of appointment should preferably be shared with independent trustees; or vested in them alone and that powers to appoint and remove trustees and beneficiaries should also be shared with independent trustees or appointers, or vested in them alone.

To illustrate this matter, reference can be made to a recent case. This is not only a typical case, but it "contains an overview of some of the other leading authorities on the point".[143] This is the case of *Commissioner for the SARS v NWK Ltd*[144](hereafter *NWK*) and it concerned a tax matter:[145]

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138 Stafford *The dangers of translocating Company Law principles into Trust Law* 121.

139 The extent to which the veil protects the assets must be certain to outsiders. They must have reasonable certainty of the exact consequences will be when working with a trust. Van der Linde 2012 *THRHR* 372 and Stafford *The dangers of translocating Company Law principles into Trust Law* 184.

140 The trust veil will be pierced if the intention of the trustee is not *bona fide* or in good faith, removing the protective veil of the trust, allowing claims from creditors and divorcing spouses to be made against the value of assets in the trust.

141 Note that the former object is not unlawful. See, for example, *Hiddingh's Trustee v Colonial Orphan Chamber and Hiddingh* 1883 (2) SC 273

142 Grant Date Unknown http://www.anthonygrant.com/trusts/55-dealing-with-property-when-it-is-in-a-trust; Stafford *The dangers of translocating Company Law principles into Trust Law* 184-185.

143 De Waal 2012 *Rabels Zeitschrift* 1081.

144 2011 (2) SA 67 (SCA) (supra n.13) par 3, 38 and 40, (*NWK* case).

145 De Waal 2012 *Rabels Zeitschrift* 1081.

> [T]he intention was to gain a tax advantage rather than really to borrow the sum of money in question. NWK, on the other hand, argued that there was an "honest intention" to execute the agreements "in accordance with their tenor" and that the claims for deductions were therefore valid. The Supreme Court of Appeal's point of departure was that the "mere production of agreements does not prove that the parties genuinely intended them to have the effect they appear to have". The question is rather whether the parties to an agreement actually intended that the agreement would have effect *inter partes* "according to its tenor" (or form); if not, effect must be given to "what the transaction really is". But how can this question be answered?

The court approached this case by referring to other leading cases that has dealt with issues similar to this in the past for authority and guidance.[146] Based on the examination of the leading cases on the subject, the court concluded that there is "two principles which appear to be finely balanced, but not in conflict".[147]

The first principle is that it is not wrong to arrange your affairs in such a way as to avoid liability in some or other form or to gain some advantage.[148] The other is that a court:

> will not be deceived by the form of a transaction: it will rend aside the veil in which the transaction is wrapped and examine its true nature and substance.[149]

This means that the court will look at the intention with which the trust was created, and secondly, they will consider substance over form, rather looking at the contents and aim of the parties and trust deed rather than the form of the trust. The case of *Zandberg v Van Zyl*[150] is a classic example of how these principles were formulated by Innes J. The decision is worth quoting in full because it specifically deals with ideas relevant to this research:

> Now, as a general rule, the parties to a contract express themselves in language calculated without subterfuge or concealment to embody the agreement at which they have arrived. They intend the contract to be exactly what it purports; and the shape which it assumes is what they meant it should have. Not infrequently, however (either to secure some advantage which otherwise the law would not give, or to escape some disability which otherwise the law would impose), the parties to a transaction endeavour to conceal its real character. They call it by a name, or give it a shape, intended not to express but to disguise its true nature. And when a Court is asked to

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146 De Waal 2012 *Rabels Zeitschrift* 1082.

147 *NWK* case (supra n.13) para 42.

148 *NWK* case (supra n.13) para 42 and De Waal 2012 *Rabels Zeitschrift* 1082.

149 This is the so-called substance-over-form-principle referred to by Geach in his presentation: Geach "Some Topical Issues relating to Trusts". It was stated that should the founder and trustee contract to a form that resembles a trust merely to enjoy the benefits that it provides to a user, but the founder does not intend for the form to actually be a trust or comply with all the relevant requirements, the court will look to the *substance* of the matter and how the affairs actually were conducted, and not to the form they wished it would take.

150 *Zandberg v Van Zyl* 1910 AD 302, (*Zandberg*).

> decide any rights under such an agreement, it can only do so by giving effect to what the transaction really is; not what in form it purports to be.[151]

What Judge Innes tried to illustrate here is that the object is to determine a person's real intention as opposed to their masked intention when creating the trust.[152] He found that if the only reason for contracting into a trust was to obtain some or other tax benefit, this trust form will be regarded as being a simulation of a trust, in other words a sham.[153] Judge Innes goes further to say that it does not matter whether the two parties act in line with their responsibilities in terms of the contract, the contract will remain a sham, and this might only be a way for them to fool the court into thinking that the contract has authority.[154]

An example of how a founder can create a sham trust is where he generates the idea that a valid trust has been created. He then uses this instrument to mislead his creditors. This is an accurate description of the exact shape that a sham trust takes on. With pretence no valid trust comes into existence because there is a lack of real intention.[155]

The consequences of having a real or masked intention with a trust differ with regard to a sham trust and the alter ego trust. A clear distinction in terms of control will be made between the two mentioned trusts in the following chapter. De Waal,[156] notes in an article that the intention with which a person creates a trust, can have an influence on the consequence once the veil has been pierced in a dispute, or if the trust is inspected due to reasonable suspicion of abuse or fraud. The first example is the result of really intending "to benefit a recipient, but not to create a trust, the supposed trust will be disregarded". The beneficiary may then accept the benefit without any burden. The second result may be summarised as follows: If the founder's intention was to create a partnership of *fiddeicommissum* for example, and not a trust, the contract will be accepted and interpreted "in accordance with the intention of the parties". The third and

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151 According to the judge all of this can be summarised in the maxim *plus valet quod agitur quam quod simulate concipitur*. See *Zandberg*.
152 *Zandberg*.
153 De Waal 2012 *Rabels Zeitschrift* 1082 and *Zandberg* par 302B.
154 *NWK* case (supra n.13) para 55 and De Waal 2012 *Rabels Zeitschrift* 1083.
155 De Waal 2012 *Rabels Zeitschrift* 1087 and also see Moffat (supra n64) 164.
156 De Waal 2012 *Rabels Zeitschrift* 1097, *NWK* case (supra n.13) para 55 and *Zandberg*.

final form of intent, namely a fraudulent one, where no real intention existed to create a trust in the true sense, no effect will be given to the contract.[157]

This topic can be concluded by noting that intention is an important determining factor. When a real or sham intention has been established, several determinations come into play. For example, if a person had a real intention to create a trust, a valid trust will come into existence. Where the founder had no intent to create a trust, but merely pretended to create one, no valid trust is created. To indicate how intent, in my opinion, could have another influence on trusts is by mentioning that it can assist the court with the distinction between a sham trust and an alter ego. If a valid trust is created, it will not be a sham. However, when a valid trust is created, but the intention and control with which it is administered tends to abuse the trust form, this can be an indication of the trust being the alter ego of a founder/trustee.

Thus, the intention with which the founder creates a trust is not the only factor that the court will consider as a requirement for piercing the trust veil. According to De Waal,[158] control and management of a trust and trust assets should also be considered. What will be evident from the next discussion is that the lack of separation between control and enjoyment of the trust assets are taken into consideration by the courts when deciding to go behind the trust form.

2.5 Control: sham, abuse and alter ego[159]

2.5.1 Introduction to control

Ownership, control and management of the trust property and vesting thereof, will depend on the type of trust and the authority assigned to the trustees. In the following paragraph the issue of control in relation to sham trusts and alter ego trusts (as a form of abuse), will be addressed in more detail.

With reference to control over trust assets it should be mentioned that a distinction can be drawn between *de facto* control and *de iure* control. Where *de iure* control asks the question of legal control and supposes that control should be in the hands of the

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157 De Waal states in his contribution that this comment is trite law and no authority is needed. However, all the courts support this approach. See further *Hippo Quarries (Pty) (Ltd) v Eardley* 1992 1 SA 867 (A) 877C-E.

158 De Waal 2012 *Rabels Zeitschrift* 1090-1093.

159 Stafford *The dangers of translocating Company Law principles into Trust Law* 23 and Trusts Unlimited Date Unknown http://www.trustguru.co.za/Legal_nature_of_trusts.html.

trustees,[160] de *facto* control focuses on actual control exercised by a trustee in terms of the trust assets and whether it is kept separate from his personal estate.[161]

However, often the founder of business or family trust appoints close relatives or friends who are willing to comply with the requests of their appointer (the founder).[162] In this instance control does not vest in all of the trustees[163] and the founder himself controls the trust, being a trustee himself.[164] *De facto* control over a trust is often associated with the alter ego or sham doctrines, thus not preferable or allowed.[165] To determine whether a party has such control it is necessary to first have regard for the terms of the trust deed and secondly to consider the evidence of how the affairs of the trust were conducted during the subsistence of the trust in issue.[166]

In some instances it might seem that a trustee has actual control over the assets or made a donation purely with the intention of frustrating the wife's or husband's claim for a redistribution order, but in terms of the trust deed, some or all of the assets are beyond the control of the founder. For instance, where assets/right to assets vests in a beneficiary, such as a charitable institution accepting the benefit or a bewind trust, thus, in reality he did not undermine the trust form and the assets will not be subject to any claims. However, if actual control did vest in the founder and he controls the assets in his name, to his advantage and, were it not for the trust he would have controlled the assets in his personal capacity, these assets may be taken into account in determining redistribution and to settle creditors' debts.[167]

From the discussion it is clear that if a trust and its assets are controlled in a *de facto* manner, the intention of the party in relation to creation of the trust is questioned. This leads to the situation where the court needs to determine whether a party controlled the

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160 According to the *Trust Act* s6, trustees are authorised in their capacity as trustee by the Master in writing, therefore his control is legally bestowed on him.

161 This is a requirement for a valid trust. *Braun v Blann* paras 345-346.

162 *Badenhorst* par 9, also refer to par 2.3 of this mini-dissertation for a detailed discussion with regards to the nature of this type of trusts.

163 More often than not the founder himself is a trustee as well, therefore it is stated that the control do not vest in *all* trustees, but only in him, as one of the trustees. Also see footnote 33 and 116 of this mini-dissertation.

164 *Badenhorst* paras 9-10.

165 Stafford *The dangers of translocating Company Law principles into Trust Law* 346.

166 *The Shipping Corporation of India Ltd v Evdomon Corporatio*n 1994 (1) SA 550 (A) par 566 and *Badenhorst* paras 9-10.

167 The court may consider piercing the trust veil and removing the protection that a trust provided for trust assets. See *Badenhorst*.

trust contrary to common law or had the intention[168] to abuse the trust form, either causing the trust to be the alter ego[169] of a trustee, or making it a sham if the person had no intention to create a trust.

2.5.2 Sham versus abuse and alter ego

It is important to distinguish between a *sham trust* and the *abuse* of a trust form.[170] The reason for distinguishing between a sham trust and the abuse of a trust form are based on the premise that the consequences flowing from each form are different. There are different results relating to what happens to the trust assets when the veil of each form is pierced.[171] Another important distinction between a sham and the abuse of a trust form, as found in De Waal,[172] is that the one trust is created as a valid trust, complying with all the general trust-requirements, but the intention and the way of controlling the trust property changes along the way and the founder/trustee start to abuse the trust form. On the other hand, a sham trust is invalid from the start. It was never the intention of parties to create a trust in the first place. De Waal[173] goes on to explain the difference between abuse of the trust instrument and a *sham trust* in a recent article published in *Rabels Zeitschrift*:

> It has been argued that sham situations on the one hand and abuse on the other, are approached from different theoretical angles. In the case of a sham, the question is whether a valid trust has been created at all. Here the emphasis falls on the requirements for the creation of a valid trust, specifically that the founder must have the intention to create a trust. In the case of an abuse situation, the premise is that there is a valid trust and ignoring the trust for a particular purpose. However, the distinction between the two situations is not only important for theoretical clarity. It also has practical implications. The most important one- is that it is decisive for the application (or destination) of the trust assets. This, in turn, has implications for both the trust beneficiaries and third parties such as trustee's spouse or private creditors.

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168 *Intention* was discussed in great detail in ch 2.4 of this mini-dissertation.

169 In order for a trust to be found a person's alter ego it must be proved that the person as the founder and/or trustee has controlled the trust solely and even derived a benefit from the trust. The founder can ensure he retains control by inserting provisions to this effect in the trust deed, by using a 'letter of wishes' to keep control or doing so through beneficiaries, of which a family or business trust is a classic example. Harding *Importance of adhering to the basic trust idea* 6-7 and Stafford *The dangers of translocating Company Law principles into Trust Law* 121.

170 Harding *Importance of adhering to the basic trust idea* 2.

171 Harding *Importance of adhering to the basic trust idea* 2.

172 De Waal 2012 *Rabels Zietschrift* 1080.

173 De Waal 2012 *Rabels Zietschrift* 1080.

Thus, a trust can only be said to be a *sham trust* when the founder/other parties never had the intention of creating a valid trust. However, Van der Linde[174] is of the opinion that it is immaterial whether the corrupt intention existed prior to the creation of the trust of arose during the existence of the trust. The intention for the trust to be a sham must merely be present from the evidence brought before the court, regardless of when the trust form was intended to be a sham. With regard to abuse of a trust, this only occurs after a valid trust has been established.

In our law it seems that the consequence for someone who abuses the trust form will be that the value of the assets, forming part of the abused trust, is added to the value of the founder/trustee's personal estate. The trust protection is then removed, making the trust assets susceptible for redistribution orders, [175] claims from creditors and even to drastic tax implications.[176] The actual assets will remain the property of the trust in right and title for the benefit of the beneficiaries. It is only the value of these assets that is taken into account by the court[177]. Although this approach by the courts is currently the only and most effective one, it will be interesting to know what their approach will be if a trustee uses the courts' judgement to his advantage. For example, if a spouse do not want his property, like a farm, to become his divorcing wife's property, he can place the specific property in a trust, in so doing abusing the trust form for protection. During the divorce, should the court find the trust to have been abused and mainly created for keeping property from the wife, the court will take into consideration the value of the property when making a redistribution to the wife.[178] The husband can easily make a loan to pay the wife the amount that the court ordered, not parting from his property because it will remain in the abused trust, it is only its value that is taken into account. The husband will be able to continue using the trust. This in effect means that an abused trust will only come under scrutiny when a claim against it arises, no further regulation or follow-up of this specific husband's trust will be conducted, allowing him to abuse the trust again after the case has been finalised. This question is left unanswered. The same uncertainty follows for a sham trust.

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174 Van der Linde 2012 *THRHR* 383.
175 Harding *Importance of adhering to the basic trust idea* 7
176 S3(3)(d) of the *Estate Duty Act* 45 of 1955.
177 This process is commonly known as *piercing the trust veil*.
178 This example is similar to the facts and finding of the court in the *Badenhorst* case.

The consequence of finding a trust to be a sham is quite different to the abuse of a trust. With a sham trust, the assets are removed from the trust, and as mentioned earlier, no effect will be given to the transaction,[179] because technically, no trust exists.[180] The question that then surfaces is what happens to these assets? Is the founder obliged to return assets he has acquired or are they attached by the court for the benefit of someone else. This trust was never a valid trust, the people operating with the assets, acting as trustees, did so falsely. This amounts to trustees not complying with the trust deed and their fiduciary duties in utmost good faith towards the beneficiaries. If the deed required three trustees and only two were present while concluding contracts in their capacity as trustees, the transaction is invalid. What will happen to the disadvantaged party and the assets acquired by the trustees?[181]

Using a trust as a *sham* is also a form of abuse, but is not classified as the same by scholars in South Africa.[182] Case law shows that South African courts are reluctant to label a trust as a *sham trust*.[183] The reason for this could be the fact that not much has been said by scholars and courts in relation to the South African law of trusts. The sham trust is also a doctrine from the English law, which has an affluent and rich law of trust and literature that deals with the topic of sham. However, not all of the provisions in English law can simply be used and implemented in our law system without qualification and amendments to make it relevant. Our academic literature and knowledge regarding the sham doctrine is limited, little to no precedents exist.[184]

If signs of abuse in a trust are present, courts only go so far as to determine that the trust form was used as an **alter ego** of a person. It is the opinion of most authors that the most common form of *abuse* is using the trust as an **alter ego**.[185] It must also be noted that there is a difference between a **sham trust** and using the trust as an **alter ego**.

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179 *Hippo Quarries (Pty) (Ltd) v Eardley* 1992 1 SA 867 (A) 877C-E and De Waal 2012 *Rabels Zietschrift* 1097.

180 De Waal 2012 *Rabels Zietschrift* 1084 and Honoré and Cameron *Honoré: The South African Law of Trusts* 119.

181 Stafford is of the opinion that in the case an innocent third party sustain monetary loss as a result of a sham trust, the party could claim with the *actio legis Aquiliae*. Stafford *The dangers of translocating Company Law principles into Trust Law* 175.

182 Harding *Importance of adhering to the basic trust idea* 2.

183 De Waal 2012 *Rabels Zietschrift* 1086.

184 De Waal 2012 *Rabels Zietschrift* 1086 and *Badenhorst* para 23 and 28.

185 Harding *Importance of adhering to the basic trust idea* 4.

Questions that are then rightly asked include: What is the difference between an **alter ego** and a **sham trust** and is this distinction necessary or even useful? The first and immediate reaction to these questions tends to be that the distinction in South African law of trusts is not significant.[186] However, when foreign law is consulted, the distinction between the two concepts becomes more pronounced. The distinction between the two are definite,[187] but until the South African courts adopt the practise to implement the doctrine of the 'sham trust' or to rule a trust to be a sham, the distinction in our courts will not be apparent and will result in the uncertainties and questions mentioned above.[188] In other countries the definition and scope of a sham has already long been established, therefore the use and extent of the doctrine is quite clear. However, in South Africa it does not seem as if courts differentiate strictly between the two and they even confuse them[189].

One of the main concerns with regard to alter ego trusts is related to the control of the trust and specifically *de facto* control.[190] The alter ego doctrine suggests that the trust is like a 'puppet' of the founder, pulling the strings to his accord. The court indicated in *Brunette v Brunette*[191] what degree of control is necessary to prove this doctrine. Chetty J stated that in practice the founder would for example place *de iure* control in the hands of the trustees, only in reality the trustees are mere puppets of the founder,[192] who continues to manage the trust assets through *de facto* control himself.[193]

Several situations have been identified which qualifies as alter ego trusts. The first instance is where assets are settled in a trust, but the trustees never have the freedom to act with the assets as they deemed fit, they were mere nominees, only doing what they were instructed to do.[194] The second instance is where trust property is used as if it is the founder's personal property instead of that of the trust.[195] Another instance is

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186 Harding *Importance of adhering to the basic trust idea* 11.
187 Harding *Importance of adhering to the basic trust idea* 4.
188 Stafford *The dangers of translocating Company Law principles into Trust Law* 68.
189 De Waal 2012 *Rabels Zietschrift* 1079 and 1084.
190 Stafford *The dangers of translocating Company Law principles into Trust Law* 121.
191 2009 5 SA 81 (SE).
192 The High Court of Australia discussed the concept of alter ego as: "an alter ego trust occurs where a person is held to have control over an express trust to such an extent that the trustees are considered to be mere 'puppets' of the defendant". *Ascot Investments Pty Ltd v Harper* 1981 148 CLR 337.
193 Harding *Importance of adhering to the basic trust idea* 18.
194 Olivier 2001 *SALJ* 224 and 228.
195 Harding *Importance of adhering to the basic trust idea* 20.

where the founder ensures that he retains most of the control over the assets by way of the trust deed or in the 'letter of wishes'.[196]

SARS has been scrutinising trusts to determine the exact scope of powers allocated to the person (who may be the founder, trustee or a beneficiary) in control of the trust assets.[197] This is due to the fact that one of the basic principles in trust law is that there must be a clear separation between control and enjoyment[198] of the assets being kept in trust, for fear the trust is nothing more than an extenuation of the estate planner in charge.[199] Determining whether an alter ego exists depends on the actual control of the trust assets. It is not entirely clear what the consequences are for a person and other parties who use a trust instrument as his **alter ego**.[200] The approach seems to be that the value of the assets will be considered by the court to repay creditors and pay divorcing spouses their share of interest in the estate.

Courts may in circumstances where the trust is abused/found to be a sham, be compelled to pierce the veil. The result of piercing the veil will cause the court to look at the reality of the situation, ignoring the protection a trust would have afforded the person in normal circumstances, leading to the declaration that the trust is in fact being administered as the alter ego of the founder or trustee.

The court cases that will be critically analysed in the chapters below, is not aimed at making a distinction between the alter ego and sham doctrines because it has not been the practise in South African courts to distinguish between the two. Regardless of this fact, reference to the distinction as seen in the English law of the two doctrines has been made in the interest of readers, even though it is firmly believed that South Africa has this unique trust law with its distinct developments according to the South African legal system's needs, and need not conform only to the trust law principles and uses of foreign law systems.[201]

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196 Olivier 2001 *SALJ* 224 227 and 228.

197 SARS may tax the trust property that is being controlled by a trustee in terms of s3(3)(d) of the *Estate Duty Act* 45 of 1955 and Harding *Importance of adhering to the basic trust idea* 7.

198 *Jordaan* paras 300I-J.

199 Roux and Strydom 2014 *Financial Law* 32.

200 Harding *Importance of adhering to the basic trust idea* 19.

201 De Waal 2012 *Rabels Zeitschrift* 1080 and Geach and Yeats *Trust law and Practice* 6.

Thus, in agreement with De Waal it can be stated that intention is not the only considering factor, but that control of the trust and trust assets will also be given attention by courts in deciding whether a trust constitutes a sham or an alter ego and if piercing of the veil is necessary and applicable.

2.6 Conclusion

This chapter discussed the legal nature of a trust and confirmed that a trust has no legal personality except for a number of instances where legislation specifically expresses that it is regarded as a juristic person in matters relating to the legislation.

Some common law requirements and other more detailed requirements of a trust were also researched. The trust form requires that there is a separation between a person's personal estate and the trust assets. This brought the discussion to the requirement that states that control and enjoyment of the trust assets must be kept separate. If the wrong type of control (*de facto*) or too much control is exercised by a person in relation to the trust assets, some problems can also arise for the controlling party because a trust can be said to be his alter ego. All of these factors are relevant to determine the founder/trustee's intention with the creation of a trust. The primary reason for creating a trust is usually for the benefit of a third party, to protect the assets for them until the right vest in the beneficiary and they can claim their portion.

The main aim of this chapter was to answer the question of what conditions may or may not be present in a trust to avoid a court from removing the trust veil that acts as a protective mechanism over the trust assets and keep them safe from claims of creditors, or even divorcing spouses who claims a redistribution in which the trust assets must be included.

The answer to this ultimate question would seem to be that the procedure the court will take is firstly to determine whether all the general/common law trust requirements have been complied with. One of these requirements is the intention to create a trust. The consequence of the court using the requirements as a starting point will be that they will be able to determine from the onset whether a valid trust has been established or not. Where no valid trust has been created, an abuse of the trust form is automatically ruled out, leaving only a sham trust to work with. While no valid trust was created and no

effect given to the transactions made in terms of this masked intention, the situation differs from abuse.

When the court has ruled out a sham and has to determine whether the trust instrument was abused in the form of using it as the trustee's alter ego, they will also refer to control. If the trustee controls the trust with actual control (*de facto*), without separating his personal estate from the estate of the trust and carrying on his business as if no trust exists, only relying on the instrument when it relates to the benefits it can provide, it can positively be stated that this specific trust is the alter ego of the trustee and that the case allows for the court to go beyond the trust protection. It is, however, clear that both have similar elements like not complying with the core idea of a trust, where either no intention exists on creation of the trust, or the lack of real intention later is revealed by the way the trust is administered.[202]

Both a sham trust and the alter ego trust have different ends to them with regard to removing the protection of a trust veil. Piercing the trust veil was not as yet discussed in much detail because in trust law there is no provision for piercing the veil when a trust is found to be a sham or subject to abuse. This doctrine is borrowed from the *Companies Act*[203] and not yet incorporated into trust law statutes. The next chapter will deal with the introduction of the doctrine of *piercing of the veil* into Trust Law, as well as how compatible this company law doctrine is with trust matters. The practise of piercing the trust veil has been exposed too much criticism from writers like Stafford,[204] who believes that a company law principle cannot be used in trust law.

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202 Harding *Importance of adhering to the basic trust idea* 19.

203 71 of 2008, (*Companies Act*).

204 Stafford contributed to this topic in his Master's dissertation titled: *The Dangers of Translocating Company Law Principles Into Trust Law.*

3 Piercing of the trust veil and the *Companies Act*

Even if the doctrine refers to instances of a corporate nature, the possibility of using it in the trust law should be established and therefore it is relevant to discuss and understand the doctrine. The reason for this is that there are suggestions to incorporate this structure into trust law. Saldulker J explains how the structure is potentially relevant to the law of trusts.[205] In *Rees v Harris*[206] Judge Saldulker discusses the legal basis on which this could be done:

> Thus, in appropriate circumstances, the veneer of a trust can be pierced in the same way as the corporate veil of a company. Consequently, where the trustees of a trust clearly do not treat the trust as a separate entity, and where special circumstances exist to show that there has been an abuse of the trust entity by a trustee, the veneer must be pierced. It follows that if a legitimately established trust is used or misused in an improper fashion by its trustees to perpetrate deceit, and/or fraud, the natural person behind the trust veneer must be held personally liable. In these circumstances, if it is demonstrated that a trustee who has *de facto* control of trust assets effectively acquired and owned such assets for his own benefit only, such assets can in appropriate circumstances be considered to be those of the said trustee.

Thus, contrary to what Stafford[207] says, there is a possibility of using a doctrine originating from the Company law in trust law.

One example of where the doctrine was entertained in the sphere of the trust law is the facts of the *Badenhorst case*.[208] The plaintiff in the *Badenhorst* case transferred all his assets to a trust and controlled it to the advantage of all his business activities. This is an exact depiction of the type of facts that will give rise to using the doctrine in company law, namely where a director or shareholder invests/disposes his assets in a company to protect them from seizure or claims by other parties. In order to prevent individuals from misusing a company in this way, the solution in company law can be found in the *Companies Act*.[209] The *Companies Act* has very strict provisions in this regard and allows courts to 'pierce the corporate veil' (removing the separate legal status of an entity) of a company to hold the person(s) behind the company personally liable where they have frustrated the payments of debt due to misuse of the company structure to cause fraud.[210] Thus the aim is to determine whether the same doctrine is useful to the

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205 Schoeman N Date Unknown https://www.schoemanlaw.co.za; De Waal 2007 *Annual Survey* 849
206 2012 (1) SA 583 (GSJ) par 17, (*Rees v Harris*).
207 Stafford *The dangers of translocating Company Law principles into Trust Law* 129-133.
208 *Badenhorst* par 4(d).
209 S20(9) and 218 of the *Companies Act*.
210 Scott-Shaw 2012 www.legalbrief.co.za/article.

trust law, where the trust veil is pierced and the trust assets deemed to be that of the controlling trustee and for the assets to be taken into consideration to satisfy claims against the owner.

3.1 Doctrine of piercing of the corporate veil[211]

It is common cause that a company exists as a legal person,[212] separate from its directors and shareholders. This separation allows for the directors and/ shareholders to have limited liability in relation to transactions that the company engage in with creditors and debtors. This means that when a creditor has a claim against the company or the company is liquidated, only the assets registered in the name of the company is available for redistribution to the creditors of the company, keeping the directors' personal estates safe from claims.[213] The separation and protection referred to here are symbolised and effected by the so-called *veil*. This protection can work the other way around as well. Often persons sell or donate their personal property to a company to benefit from the protection mentioned above. A company's protection works on the same basis as that of a trust, as soon as creditors institute claims from this person or at the instance of insolvency, the debt must be settled from the property in his estate. No claims can be made in terms of the property in the company, it legally belongs to the company, and the veil keeps all property behind it safe:

> The corporate veil, then, is a fundamental aspect of company law and is a protective device for those who exist behind it.[214]

Thus, the company entity resembles the trust instrument to some extent in terms of the protection it renders to trust assets. However, there are certain instances[215] like abuse[216] where the courts will "ignore the limited liability of the company" and go on to pierce the

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211 Reference to the doctrine of piercing of the corporate veil or piercing of trust veil will from hereinafter be referred to as only 'the doctrine'.

212 The legal nature of a company is different from the nature of a trust. However, ch 2 showed that for some legislative provisions a trust is deemed a legal person, and the Companies law is one of those. Thus, the question is why can the doctrine can in principle not be used in trust law. Both have a veil, a trust protecting trustees is the same as the directors of a company. Also look at ch 3.3.

213 Unless the trustee has signed an agreement of standing personal security for the trust.

214 Stafford *The dangers of translocating Company Law principles into Trust Law* 126 and also see Hawke *Corporate Liability* 126.

215 Schoeman N Date Unknown https://www.schoemanlaw.co.za

216 S 20(9) of the *Companies Act*.

corporate veil,[217] ultimately rejecting the separateness of the two estates. This was confirmed in the *Kurt Robert Knoop v Birkenstock Properties (Pty) (Ltd)*:[218]

> The corporate veil may be pierced where there is proof of fraud or dishonesty or other improper conduct in the establishment or the use of the company or the conduct of its affairs and in this regard it may be convenient to consider whether the transactions complained of were part of a "device", "stratagem", "cloak" or a "sham".

The consequence flowing from this is that the persons and property behind the veil will become liable for claims against them or the company. According to Schoeman[219] the doctrine has been applied in abused matters outside the commercial field.[220] The aim was to eliminate instances where a corporate structure, like a company, is used to avoid legal responsibilities. The court, in confirmation of this, sounded a clear warning to every director/shareholder of a company, emphasising that those who are found guilty of abusing the corporate figure will not be dealt with lightly.[221]

The deciding factors for a court when considering whether to pierce the corporate veil is a "balancing exercise".[222] The court will consider all relevant factors before piercing the veil. Based on the merits of each case before the court, it will decide whether it is necessary and fair to ignore the separateness of the person and company, allocating liability to them in justification. The newly incorporated *Companies Act* ventures to supplement the common law notion of piercing the veil to the extent that in section 20(9), it specifically provides a platform for aggrieved parties (creditors, employees, trade unions and shareholder), who stand victim to the abuse of companies by directors and allow them to claim damages in terms of section 218(2) for the loss that they have experienced.[223]

The foundation for the doctrine has been established by company law, and is it not necessary to reinvent the wheel. Therefore the well-established provisions can be used

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217 Piercing of the corporate veil is a common law notion, which is now supplemented and expanded by the new *Companies Act.* Sakutukwa 2013 www.rsmbettyanddickson.co.za

218 2008 3 SA 67 (A), (the *Knoop* case), delivered in terms of the new *Companies Act* and *The Indian Shipping Corporation of India Pty Ltd v Evdomon Corporation* 1994 1 SA 550 (A), (*The Indian Shipping Corporation case*)

219 Schoeman N Date Unknown https://www.schoemanlaw.co.za

220 Such as trust law. In all the mentioned cases concerning trusts, the issue of piercing the corporate veil was something the court had to address.

221 *Cape Pacific Ltd v Lubner Controlling Investments Pty Ltd* 1995 4 SA 790 (A).

222 Schoeman N Date Unknown https://www.schoemanlaw.co.za

223 *Companies Act* and Sakutukwa 2013 www.rsmbettyanddickson.co.za.

as is by simply modifying the terms so that it is applicable to trusts. The possibility will be investigated in the following paragraphs.

3.2 Introduction of the doctrine to Trust Law

For the legislature to adopt the doctrine into trust law, there are two sections that will possibly have to be included in the *Trust Act* together with the doctrine, namely section 20(9) and 218 of the *Companies Act*. According to section 20 (9) of the new *Companies Act* the court may:

> on application by an interested person or in any proceedings in which a company is involved, a court finds that the incorporation of the company, any use of the company, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity.

Obviously, *company* will be replaced with *trust* when this provision is adopted or written into the existing legislation that governs trust law, such as the *Trust Act*. The provision will ensure that the aggrieved parties have the right in terms of legislation to bring an application before the court for piercing the trust veil when it has been abused by the trustees, allowing the protection of trust users, as well as innocent third parties dealing with trusts.

Furthermore, section 218 of the Companies Act gives *locus standi* to "any interested party such as creditors, employees, trade unions, shareholders and so on".[224] These parties can now claim damages and the cost they incurred as a result of the abuse of a company. Thus, in terms of this provision forming part of the trust law, section 218 is an important provision. The provision assists persons who transact with trusts so that they have a remedy should the trust be a product of abuse.

During the appeal trial in the well-known case of *Parker*,[225] the Supreme Court of Appeal under leadership of Cameron JA made a ruling that changed the future of trusts. The court noted that trust instruments are becoming browbeaten in practice due to the protection that a trust offers to both a user and the assets.

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224 Schoeman N Date Unknown https://www.schoemanlaw.co.za

225 A ratio supported by Binns-Ward J in the *Van der Merwe* case and Stafford *The dangers of translocating Company Law principles into Trust Law* 126.

Given the extensive exploitation of the trust form, Cameron JA reasoned that both a remedy for victims and retribution against the abusers have to be sought to curb the abuse:

> [I]t may be necessary to extend the well-established principles of company law into trust law. In particular, the court felt it necessary to import the doctrine of piercing the corporate veil from company law into trust law.[226]

Some may view the gesture of borrowing a doctrine from company law as going a bit overboard or even wrong.[227] However, this doctrine was employed under company law to restrict abuse of companies by directors for the limited liability that the instrument offered. The doctrine derived from common law[228] allows the courts to use their discretion to determine when they will go beyond the veil to protect innocent third parties dealing with the entity. It can be argued that Cameron JA suggested the doctrine's use in trusts for the exact same reasons.

Currently, trust law is experiencing the same problems that company law experienced in terms of the abuse of a financial planning instrument. It can therefore be bluntly stated that while the doctrine was utilised for curbing the abuse,[229] it can now, only in relation to trusts, be used by courts in trust law to protect third parties like the creditors of an insolvent trustee or a divorcing spouse who was tricked out of his or her portion of the estate.

The application and outcome of the doctrine in trust law give courts more discretion to determine when they can pierce a trust veil and when not.[230] Cameron JA further held that:[231]

> should the conduct of a trustee invite the inference that the trust form was a mere façade for the conduct of a business "as before", and that the assets allegedly vesting *de iure* in the trustees in fact belong *de facto* to one or more trustee, the veil will be

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226 *Parker* case and Stafford *The dangers of translocating Company Law principles into Trust Law* 126.

227 Stafford is of the opinion that: "South Africa's interpretation and application of these doctrines in trust law, and reveals the erroneous judicial development in which the courts have in some instances mistakenly replaced the sham doctrine with the company law doctrine of piercing the corporate veil or, in other instances, have erroneously conflated the two trust doctrines". See Stafford *The dangers of translocating Company Law principles into Trust Law* iii.

228 Geach "Some Topical Issues relating to Trusts" and Schoeman N Date Unknown https://www.schoemanlaw.co.za

229 *Knoop* case and *The Indian Shipping Corporation* case.

230 Stafford *The dangers of translocating Company Law principles into Trust Law* 126.

231 *Parker* case.

lifted, and the trust property which was once protected by the trust will become susceptible to the claims of third-party creditors.

The doctrine is applied in trust law to the same effect as in company law.[232] It is still to some extent unclear what the guidelines are according to which the court will decide whether or not to pierce the veil in trust law. The case law that will be discussed at a later stage reveals that the veil is pierced at the instance of abuse. This could possibly be the determining factor, similar to the *gross abuse* necessary for piercing a company's veil.[233] Well-defined determining factors for companies have been set out in section 20(9).[234] As will be expounded at a later stage, the courts will use this doctrine in trust law as a last resort and only in exceptional cases.[235]

The rationale for the doctrine in company law has already been established, and the grounds for piercing the veil in company law have been discussed in depth. It was further mentioned that the introduction of the doctrine to trust law was relatively easy and effective, providing a remedy to aggrieved parties who are dealing *bona fide* with trusts. Sadly, some people are opposed to change, especially if the outcome of the change is unknown or uncertain. This might likely explain why there is quite a bit of criticism against the use of a company law doctrine in trust law.[236] The following section offers a comparison of a company and a trust to illustrate why and how this doctrine can be borrowed and applied without negative repercussions.

3.3 Comparison between trust veil and corporate veil

The point of departure for this discussion is that piercing of the veil has always been regulated by common law.[237] Only recently did the *Companies Act* make reference to it

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232 Scott-Shaw 2012 www.legalbrief.co.za/article

233 S20(9) of the *Companies Act*.

234 From case law it can be gathered that each case is tried on its own merits and facts. In Ex Parte Gore 2013 2 SA 437 (WCC), (Ex Parte Gore), the court was faced with the first case that required them to interpret s20(9) since the new *Companies Act* had been incorporated. The judgement sent a clear warning that "the **corporate veil will be pierced** where **unconscionable abuse of juristic personality** of a company **is found,** including in company groups and that the **remedy will not be regarded as an exceptional one to be used only as a last resort.** It appears that the statutory remedy of piercing the corporate veil would be applied by courts with less reticence than the common law remedy" (Own emphasis).

235 *Rees v Harris*.

236 Stafford clearly conveys his disagreement with how South African Courts apply the sham, alter ego and piercing the veil doctrines in his master's dissertation: *The dangers of translocating Company Law principles into Trust Law*.

237 Cassim 2013 *De Rebus* 51, Geach "Some Topical Issues relating to Trusts" and Schoeman N Date Unknown https://www.schoemanlaw.co.za

in statutes.[238] Before the incorporation of the 2008 *Companies Act*, an application for piercing the corporate veil had to have been brought in terms of the common law. However, the *Companies Act* now grants courts the statutory power to pierce the veil if they find evidence of "unconscionable abuse" or "gross abuse".[239]

South Africa, through the assimilation of English law and Roman-Dutch law, together with the refinement of these rules by the courts and the Legislature, has developed a genuinely hybrid and well-respected law of trusts. Geach and Yeats note that "the common law in South Africa, together with good practice that has developed over the years by practitioners and trust companies, currently forms the cornerstone of the law of trusts in South Africa."

Although the new *Companies Act* does not list the exact circumstances that warrant piercing of the corporate veil, it makes reference to broad terms like "unconscionable abuse" and "gross abuse", which, if present, allow for piercing of the veil.[240] A recent case dealing with these terms found in section 20(9) of the *Companies Act*, is the *Ex Parte Gore* case, where the court held that: "where accounting disregards juristic personality, so too will the law".[241] It is in the same judgement that the question was asked whether section 20(9) overrides the common law.[242] It was found that the relevant section in the *Companies Act* does not override the common law or the way in which it warrants piercing the corporate law. In fact, it was stated that the principles of the common law with regard to piercing the veil should act as a guideline for courts when referring and interpreting section 20(9). It was further held that the courts should interpret the *Companies Act* in such a way that it gives effect to the purpose of the act. The court therefore stated:[243]

> It is unable to identify any discord between section 20(9) and the approach to piercing the corporate veil evinced in cases decided before it came into operation.

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238 Piercing of the corporate veil is now a statutory remedy, adding weight to its application and effect.
239 S20(9) and s218 of the *Companies Act*.
240 Courts are granted a wider discretionary power in terms of s20(9) of the Companies Act. Also see Sakutukwa 2013 www.rsmbettyanddickson.co.za and *Ex Parte Gore* para 32.
241 Cassim 2013 *De Rebus* 51.
242 Cassim 2013 *De Rebus* 51 and *Ex Parte Gore*.
243 *Ex Parte Gore* par 32.

Given that there are no defined categories of cases when a court will pierce the corporate veil based on common law,[244] the court held that the correct way to see the relationship is that section 20(9) is *supplemental,* rather than *substitutive* of the common law.[245]

It is Stafford's[246] opinion that the court takes many approaches to veil-piercing of trusts. He says that the approach most often used is the categorisation approach, which he describes as an approach that was established by the courts themselves. There are various categories that must be considered before deciding to pierce the veil. Those categories include *in the interests of justice*, *equity*, *alter ego*, *fraud* or *improper conduct* and *agency*.[247] Based on the equity category, the *Van der Merwe*[248] case revealed the following:[249]

> The abuse of the trust form is something that should not lightly be countenanced by the courts in cases in which the veneer of a trust is used to protect the trustees against fraud and dishonesty and to raise unscrupulous defences against bona fide third parties seeking to enforce the performance of contractual obligations purportedly entered into by such trustees ostensibly in that capacity..In Parker, Cameron JA ventured the following observations in this connection: The courts will themselves in appropriate cases ensure that the trust form is not abused. The courts have the power and the duty to evolve the law of trusts by adapting the trust idea to the principles of our law (*Braun v Blann and Botha NNO and another*).This power may have to be invoked to ensure that trusts function in accordance with principles of business efficacy, sound commercial accountability and the reasonable expectations of outsiders who deal with them, and 'Where trustees of a family trust, including the founder, act in breach of the duties imposed by the trust deed, and purport on their sole authority to enter into contracts binding the trust, that may provide evidence that the trust form is a veneer that in justice should be pierced in the interests of creditors.' A decision to disregard the veneer would, like one to pierce the corporate veil, be a decision to afford an equitable remedy.

Van der Linde[250] stated that the court probably relied on how equity evolved in the English law of trusts by examining the test[251] the English courts did to determine whether piercing the veil was a remedy available to the case.[252]

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244 *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd and Others* 1995 4 SA 790 (A).
245 *Ex Parte Gore* par 34 and Cassim 2013 *De Rebus* 51.
246 Stafford *The dangers of translocating Company Law principles into Trust Law* 127.
247 Stafford *The dangers of translocating Company Law principles into Trust Law* 126.
248 2010 5 SA 555 (WCC).
249 Paras 570B-G.
250 Van der Linde 2012 *THRHR* 377.
251 See also *Badenhorst*, Harding *Importance of adhering to the basic trust idea* 47 and Van der Linde 2012 *THRHR* 379.

3.4 Conclusion

In foreign law a sham has to exist to justify piercing, and this is the only instance when a trust may be pierced according to foreign law. In South African law a sham is not pierced.

Harding[253] suggests that piercing the veil of a trust can be a solution for curbing the abuse of a trust form. Case law reveals that the most common consequence for a person who is found to abuse a trust is piercing of the veil (see chapters 4 and 5). However, piercing the veil is only possible when a trust[254] is found to be an alter-ego trust, and not when a trust is a sham trust. Stander[255] explains the implications of veil-piercing for a trustee as follows:

> The court referred to the *Turquand* principle and the principle of "piercing the corporate veil". The motivation is that assets allegedly vesting in the trustees of a trust, in fact belong to one or more of the trustees personally. This view may have obvious and important implications in case of the sequestration of the trustee's estate. It implies that the assets concerned may be used in satisfaction of the trustee's debts because "in fact it belongs to the trustee". However, it may also be used in satisfaction of debts "to the repayment of which the trustees purported to bind the trust". Thus, if the trust's estate is sequestrated, the assets may be used in satisfaction of the trust's debts. If the personal estate of the trustee is sequestrated, these assets may be utilized in satisfaction of the trustee's personal debts. Consequently it is relevant to ask the question whether the trustee's personal estate (irrespective of sequestration) would be liable for restitution in favour of beneficiaries for these actions in breach of trust in competition with the creditors of the trustee.

What Stander[256] has said may be a warning to trustees to be careful of the consequences of piercing the veil. The effects are seriously detrimental to a trustee should it be found by courts that he has abused the trust.

In agreement with Harding[257], it can be concluded that it does not matter what test the court decides to use, it comes down to the same result because both methods question the *intention*[258] of creating the trust. Thus, to finally decide whether the remedy is applicable, the courts will need to establish if this trust is an alter ego of the trustee, as

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252 "The guiding criterion was whether it would have led to *unjust* or *inequitable results* if a remedy were refused in a particular situation…" Van der Linde 2012 *THRHR* 378.
253 Harding *Importance of adhering to the basic trust idea* 46.
254 Harding *Importance of adhering to the basic trust idea* 46.
255 Stander 2008 *INSOL.* 165.
256 Stander 2008 *INSOL.* 165.
257 Harding *Importance of adhering to the basic trust idea* 48.
258 See ch 2.4 for an in-depth discussion of the *intention* requirement.

well as whether clear separation between enjoyment and control was exercised.[259] This remedy is a good deterrent to avoid abuse, as the consequences of this remedy is expensive and detrimental when applied. Some writers are of the opinion that this remedy is successful in its purpose to prevent abuse and must therefore be implemented as legislation.[260]

For the next matter, namely piercing of the trust veil where the matter concerns insolvency of a trustee,[261] the case of *Knoop NO and others v Birkenstock Properties (Pty)*[262] and the *Parker case* will serve as illustration. The enquiries by third parties as to when a court will pierce a 'trust veil' to prevent an individual from frustrating the claims of creditors are also considered.

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259 *Knoop par* 26.

260 Harding *Importance of adhering to the basic trust idea* 47 and Vorster *Misbruik as gevolg van die miskenning van die besigheidstrust* 63.

261 See ch 4 Piercing the trust veil with regards to insolvency matters.

262 *Knoop* case.

4 Piercing the veil with regard to insolvency matters

As soon as a founder is declared insolvent in his personal capacity, all the assets he transferred to the trust prior to his insolvency are free from the claims of his creditors.[263] However, given this protection, people started abusing the trust veil,[264] consciously frustrating claims of creditors by transferring assets to a trust when they expect insolvency or in the instance of divorce.[265]

Following beneath are cases that will help to clarify the option of piercing the veil with regard to matters of insolvency and how the court approaches such cases.

4.1 Parker case

4.1.1 Facts[266]

In 1992 Mr Parker created a trust, assigning himself, his wife and their lawyers as trustees. The beneficiaries were Mr and Mrs Parker and all their descendants. The trust deed held that there should always be three trustees in office, and when the lawyer resigned as trustee in 1996, the two remaining trustees neglected to appoint a third trustee. During this time of only two trustees in office, they continued to enter into agreements, also with the applicant in the case, who insisted on the third trustee's appointment. Mr and Mrs Parker appointed their son, who is also a beneficiary, as the third trustee. Regardless of this appointment, the son was never involved in any trust matters or recognised in any decision-making. The applicant obtained a sequestration order in court *a quo* against the trust, as well as the trustees personally, in satisfaction of their debt, amounting to sixteen million rand.

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263 Important provisions in this regard is s8(c), s26(1)(a) and s26(1)(b) of the *Insolvency Act* 24 of 1935. These sections provide for: "Every disposition of property not made for value may be set aside by the court if such disposition was made by an insolvent— (a) more than two years before the sequestration of his estate, and it is proved that, immediately after the disposition was made, the liabilities of the insolvent exceeded his assets; (b) within two years of the sequestration of his estate, and the person claiming under or benefited by the disposition is unable to prove that, immediately after the disposition was made, the assets of the insolvent exceeded his liabilities: Provided that if it is proved that the liabilities of the insolvent at any time after the making of the disposition exceeded his assets by less than the value of the property disposed of, it may be set aside only to the extent of such excess". Consequently, if the court is satisfied that the transfer of assets was to frustrate the creditors, the disposition may be set aside by the court.

264 See "newer type of trust" that was discussed earlier in ch 2.

265 See ch 4.

266 Paras 78A-F.

However, the court went ahead and set aside the sequestration orders against the Parkers, whereupon the appellant approached the Supreme Court of Appeal.

4.1.2 Judgement

It was held that when a trust deed requires the consent of all the trustees to conclude a transaction, a transaction that did not have the consent of all the trustees, is not valid, thus the loans made in the *Parker* case were found invalid.

Cameron JA once again seized the opportunity to remind trustees of the importance of separating enjoyment and control of trust assets.[267] He stated that the main idea of a trust is to secure and properly administer property for the benefit of beneficiaries, and this is why a trustee cannot be the only beneficiary. The situation where the trustee is the only beneficiary is contrary to the basic trust idea and consequently no trust is formed.[268] The basic trust idea is therefore based on the premise of separation, constantly emphasised by courts. It is due to the separation of estates, control and enjoyment that the trustee can objectively administrate the trust. An independent trustee will make decisions for the benefit of the beneficiaries because such a trustee has no interest in benefitting himself. This means that the trustee will not enter into transactions that can be found invalid at some stage.[269]

The court further held that when a trust is properly structured, for example making a clear distinction between ownership and control, outsiders who are dealing with a trust have the consolation that the transaction is valid. Where the trustees are the sole beneficiaries, they will have no interest in whether the trust is administered correctly or a transaction is valid, they just wish to benefit by hiding behind the trust veil, continuing their business as usual.[270] The Supreme Court of Appeal allowed the appeal to succeed for several reasons as quoted below:[271]

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267 Par 86E: "The core idea of the trust is the separation of ownership (or control) from enjoyment".

268 Par 86F.

269 Paras 87C-E.

270 Par 89C: *"*As trustees who were simultaneously the principal beneficiaries the Parkers had an interest in obtaining loans from the bank; as beneficiaries they had a simultaneous interest in contesting their repayment. The other beneficiaries were scarcely likely to have distinct interests: They were even more unlikely to hold the Parkers accountable for their breaches of trust in concluding the unenforceable transactions.*"*

271 Harding *Importance of adhering to the basic trust idea* 47.

(a) Despite the trust deed being clear on the number of trustees to be appointed at any given time, the trust suffered from incapacity as a result of the deficient number of trustees in office, and could therefore not act on its behalf.[272]

(b) The trust could not be bound by any transaction if it did not comply with formal requirements set out by the trust deed. Consequently the Parkers had committed a breach of trust by conducting transactions under this state of affairs and then later trying to avoid liability for the trust.[273]

(c) Neglecting to consult with their son as co-trustees in trust affairs resulted in a further usurpation of their duties as the trust deed was clear that trustees should act jointly.[274]

(d) After being placed under final sequestration the Parkers ceased to be trustees in terms of section 150(3) of the *Insolvency Act*[275] and could therefore not sign a petition for leave to appeal to the Supreme Court of Appeal.[276]

In this case, it is clear that the Parkers failed to adhere to the basics of a trust. Not only did they not comply with the trust deed, which they drew up themselves, with regard to appointing a new trustee, they also failed to distinguish between enjoyment and control of trust assets.

This case shows the trust as the alter ego of the trustees due to the lack of separation, the basic trust principle. The court did not address the possibility of the trust being a sham, since no evidence was lead in court regarding the real intention of the parties to form a trust, which is the ultimate determining factor to conclude that a trust is a sham.[277] Kloppers[278] offers and in-depth analysis of this case and concludes with some lessons to be learned:

> Een van die belangrikste lesse uit bogenoemde uitspraak is dat sowel die trustees as die partye wat met ‘n trust besigheid doen, hulself deeglik moet vergewis van die bepalings van die trustakte ten opsigte van handelinge verrig deur die trustees. Daar moet veral *gelet word op bepalings wat die minimum getal trustees voorskryf.* Indien, soos *blyk uit die feite van hierdie saak, die getal trustees benede die vereiste minimum getal daal, moet die partye met wie die trust besigheid doen daarop aandring dat die getal trustees aangevul word* tot die vereiste minimum getal…Die tweede belangrike les wat uit die uitspraak na vore kom, is die feit dat *trustees onafhanklik in hulle optrede moet wees en dat daar ‘n duidelike onderskeid tussen beheer van die trustbates en die genot daarvan moet wees.* In hierdie opsig is dit reeds praktyk by verskeie meesterkantore om te vereis dat ‘n onafhanklike trustee aangestel word.

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272 Harding *Importance of adhering to the basic trust idea* 47 and also see *Parker* par 78G.
273 Harding *Importance of adhering to the basic trust idea* 47 and also see *Parker* par 78H.
274 Harding *Importance of adhering to the basic trust idea* 47 and also see *Parker* par 78I.
275 Act 24 of 1936 and Harding *Importance of adhering to the basic trust idea* 47.
276 Harding *Importance of adhering to the basic trust idea* 47, and also see *Parker* par 78I.
277 *Parker* case and Harding *Importance of adhering to the basic trust idea* 28.
278 Kloppers 2006 *TSAR* 422, own emphasis added.

Harding is of the opinion that when these lessons are learnt and lived by, certainty is created, and a trust would be less likely to be abused by a trustee since the trustee would know what not to do.

The unanimous decision by the Supreme Court of Appeal concluded that it is possible to extend the doctrine of piercing the veil to trusts where trustees have shown a lack of separation of control and enjoyment of trust assets.[279] This has the consequence for trustees that they are held personally liable for their breach of duty of acting in the best interest of the beneficiaries of the trust. It has been heard that the trustees' breach of duty can be tied with a delictual claim if any damages or losses have been suffered by the beneficiaries, unless the cause for the loss was not the fault of the trustees. It is the opinion of the author that Cameron JA was brave in his judgement when he decided that piercing the corporate veil doctrine should be extended to trusts. In response to the criticism that principles cannot simply be lent or extended to another branch of law, consideration should be given to the fact that this doctrine, although it has always been entertained the company law sphere, is not restricted to this sphere. It is a doctrine deriving its application from the common law and providing a remedy for the abuse of the company. The same type of remedy is required for the current abuse in trust law. Will it not be effective and probably most successful if the working doctrine is extended and possibly altered to be applicable to trusts and used in the trust sphere as a remedy for the same problem? Finally, this case has set the pace for piercing a trust veil and this has caused the ripple effect that we see in all the judgements after *Parker*. This is a great remedy for creditors who are defrauded from claiming the debts owed to them by someone who transferred all his assets in anticipation of his insolvency.

4.2 Van Zyl v Kay[280]

4.2.1 Facts

The applicants in this case were the provisional trustees of the sequestrated estate of Kaye. They applied to the court to order that the assets of the JGN Trust and the company of which Mr Kaye was the sole director form part of his personal insolvent

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279 *Parker* par 29.
280 *Van Zyl v Kaye* 2014 4 SA 452 (WCC), (*Van Zyl v Kaye*).

estate. The trustees based their application on the argument that Kaye used the trust as his *alter ego* and simultaneously branded the trust as a sham.[281]

The judge, however, held that a sham and an alter ego trust are essentially different forms of abuse and that it is not possible to refer to one entity as being both.[282] He confirmed that the two terms are used interchangeably and this causes confusion among those dealing with trusts. He reminded the applicants that a sham trust does not bring about a valid trust, and therefore there is no veil to *go behind*.[283]

4.2.2 Judgement

The judge acknowledged that in the case of maladministration of a valid trust over vested trust property, a trust is not rendered legally invalid or non-existent:[284]

> The maladministration of an asset validly vested in a properly founded trust does not afford a legally cognisable basis to contend that the trust does not exist, or that the asset no longer vests in the duly appointed trustees. Thus, for the applicants to be able to establish that the Cape Town property does not vest in the Trust they have to prove that the Trust was a sham.

The onus rests on the applicants to prove that the property never vested in the trust from the beginning, causing the trust to be a sham and invalid. For the court to declare a trust a sham, some of the requirements for the formation of a trust should be unmet, and the "appearance of having met them was in reality a dissimulation".[285] Summarily, a sham indicates that no valid trust ever existed. The provisional trustees wrongly worded their argument when they stated that Mr Kaye administered the trust as his alter ego and therefore the trust should be regarded as a sham. It has already been established that one trust cannot be both.

On this note, Binns-Ward stated that there were no facts before the court to find that the JNG Trust was not founded on all the requirements and therefore property was vested in the trust validly, consequently no sham trust was created. The court found that the veil will not be pierced either, based on the argument that the trust was the alter ego of Mr Kaye and that the immoveable property will not form part of the insolvent's personal

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281 "The allegedly delinquent discharge by trustees of their responsibilities in the current case, thereby allegedly giving Kaye sole and unfettered *de facto* control of the Trust's asset gave rise to the accusation by the applicants in their founding papers that the trust was a 'sham'". *Van Zyl v Kaye* par 459 and Anon 2014 *De Rebus* 47.

282 Waar in die uitspraak?

283 Anon 2014 *De Rebus* 47.

284 *Van Zyl v Kaye* par 459J.

285 Anon 2014 *De Rebus* 47.

estate. In contrast to a sham, going beyond the veil entails that a valid trust did come into existence, but the entity is ignored, exposing what was ordinarily protected under a trust. Consequently, trustees can become personally liable for their actions regarding the trust, even if they acted in their capacity as trustee. Alternatively, the trust and its assets can be exposed to claimants if trustees acted outside the limits of the trust deed.

Piercing the trust veil often offers a reasonable and just remedy for the party that has been detrimentally affected due to the abuse of the trust form by the trustees when they tried to avoid obligations and evade liabilities like taxes. This remedy will only be granted by the courts in "suitable or appropriate cases".

Due to the fact that this is a relatively new case, little to nothing has been written about it. The aim of this dissertation is not to critically analyse and criticise the case, but to evaluate the case in so far it is relevant to this research.

In contrast to a sham, an alter ego trust entails that a valid trust did come into existence,[286] but the entity was abused in terms of its control and administration. These circumstances in general warranted the piercing of the veil. While the court said that no concrete evidence was placed before it to pierce the veil and ignore the protection, exposing what was ordinarily protected under a trust, the approach to this decision is critical.

The approach of the court in this case was different from the previous case of this nature. In all the trust related cases, whether insolvency or divorce matters, the court always first determined whether a trust was a sham or an alter ego of the trustees by taking into consideration the way the trust was administered and controlled by the trustee. Once established, the court will decide to pierce the veil of an alter ego trust if it found it just and equitable to do so. However, in *Van Zyl v Kaye*, the argument before the court was that Kaye's trust was his alter ego and therefore also a sham, and therefore the trust veil should be pierced. The court said that no compelling evidence that a sham trust had been created was brought before the court, and therefore they did not pierce the veil. The author argues that the court was correct in their approach in that a sham trust cannot be pierced because no valid trust had been created in the first place, and if there is no trust, there is no veil to pierce. However, the trustees who

[286] Refer to ch 2.5 for the distinction between a **sham** and an **alter ego** trust.

incorrectly labelled the trust as both a sham and an alter ego, should not have done so. It could cause confusion and legal uncertainty.

4.3 Conclusion

In agreement with Kloppers[287], the important factors that surface in *Parker* are that a trustee and/or founder must ensure that all the essential requirements of the trust are met, and secondly, there must be a clear distinction between the control and enjoyment of trust assets. If the essentials are not present, a trust can be regarded as being a sham. However, where a trust complies with essentials and are considered valid, but trustees abuse the form by not separating trust assets from personal assets, the trust can be regarded the founder's alter ego and might result in the court piercing the veil, as became evident from *Parker*. The consequences of piercing the veil have already been discussed in full, but it is worth mentioning the crux again briefly. When the trust protection is removed or a trust is found to be the alter ego of a trustee, as in the cases of *Parker*, the court will allow creditors to claim the debt that the trustee agreed to in his personal capacity, from the assets in the trust[288]. The court then no longer affords the trust the protection that trusts generally enjoy because the founder has abused the trust to hide assets from creditors, administering the trust and personal assets as one. The *Van Zyl v Kaye* might still be cause for many debates with regard to the trustees referring to a sham trust and considering the piercing thereof, which is contrary to the general procedure the courts follow.

The next chapter of the paper focuses on case law in relation to different instances of divorce and how trusts were abused in these instances to protect the founder of the trust from a divorcing spouse. Interestingly, it can be noted from all the relevant cases that the majority of local alter ego or abused-trust cases revolved around matrimonial proceedings.[289]

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287 Kloppers 2006 *TSAR* 422.

288 Stander 2008 *INSOL.* 165: "This view may have obvious and important implications in case of the sequestration of the trustee's estate. It implies that the assets concerned may be used in satisfaction of the trustee's debts because 'in fact it belongs to the trustee'. However, it may also be used in satisfaction of debts 'to the repayment of which the trustees purported to bind the trust'. Thus, if the trust's estate is sequestrated, the assets may be used in satisfaction of the trust's debts. If the personal estate of the trustee is sequestrated, these assets may be utilized in satisfaction of the trustee's personal debts".

289 Stafford *The dangers of translocating Company Law principles into Trust Law* 109.

5 Piercing the veil with regard to divorce matters

It is possible for a spouse[290] who is contemplating divorce to quickly create a trust and transfer the excess of their estate to the trust. The trustees subsequently take ownership of the assets transferred to the trust and it no longer belongs to the other spouse.[291] During the trial and the process of the redistribution of assets, the court considers the joint estate or even one spouse's estate and accordingly divides the assets so that both spouses benefit equally from the marriage and accumulation of assets.[292] However, when the erring spouse transfers some of the assets of the estate to a trust, that person reduces the value that the other spouse can become entitled to unfairly, especially if the claiming spouse contributed to the growth of assets in the estate or trust. Thus, when one spouse is detrimentally affected by the assets being kept away from him or her, such a spouse can apply to the court to *pierce the veil*[293] of the other spouse's trust due to the abuse of the protective veil. In the following cases it will become evident that the court will in certain matters, if facts of abuse are present,[294] pierce the trust veil on application of a spouse. The consequences flowing from piercing the veil by a court will also be discussed here.

5.1 Badenhorst v Badenhorst[295]

5.1.1 Facts

Although the *Badenhorst* case mainly dealt with divorce matters, it also influenced on the trust law. Mr Badenhorst filed for divorce against Mrs Badenhorst, who in reply claimed redistribution[296] of the estate so that the assets of the family trust and their testamentary trust, which were used as their personal assets, could be taken into consideration when determining the value of the redistribution. Evidence was given in court by Mrs Badenhorst that the trusts were set up specifically to protect the family assets from creditors, and the assets must be regarded as personal assets of the plaintiff. It was plaintiff's alter ego, she contested. She further alleged that she

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290 The wife can be the aggressor too, or it can be a gay or lesbian marriage, therefore no reference is made to husbands and wives.
291 Refer to ch 2 for an in-depth discussion regarding the legal nature of a trust and *Badenhorst*.
292 This is the so-called forfeiture of benefits of marriage.
293 This doctrine was discussed in detail in ch 3.
294 See ch 2.3 regarding abuse and *alter ego*.
295 *Badenhorst* case.
296 In terms of the *Divorce Act* 70 of 1970.

contributed just as much effort and talent into growing the trust as he did, and were it not for the trust, all the assets would have been that of the plaintiff.[297]

5.1.2 Court a quo's judgement

The question whether the trusts were created as the alter egos of the Badenhorst family was answered by the court, which referred to the circumstances surrounding the trust in terms of its legal nature, abuse of powers by the founder/trustees, and control. The court reasoned that:

> The Jubilee Trust is a separate legal entity which stands to benefit her own children. If Mr De Villiers meant in his submission that I must regard it as a separate entity and yet take into account that the plaintiff had unlimited access to it, I have grave difficulties with this reasoning. It is contradictory. It implies that I must make an adverse order against the trust via the back door. Simply put I must order the plaintiff to transfer an amount of R946 046.50 to the defendant. The defendant will in turn, thus, have her estate increased to the net value of R 1 924 366.50. That of the plaintiff reduced to R946 046.50. Because the plaintiff has unlimited access to the Jubilee Trust, even if he cannot raise this amount from his own assets, so proceeds this reasoning, he should be able to access trust property to satisfy this order. In my judgement, unless I find the trust to be a sham, I cannot make an order like this. When I find the trust to be such, I hope I will make a clear order to this effect.

He concluded by saying[298] that the trust "...was not a vehicle through which the plaintiff protected himself",[299] thus the assets did not form part of the estate for redistribution to the wife. If the husband did control the trust as his alter ego[300], the control requirement is satisfied and the assets in the trust would form part of the estate for redistribution in terms of a divorce order. This was the approach in *Grobbelaar*[301] as well as *Jordaan*[302].

5.1.3 Supreme Court of Appeal's judgement[303] *and consequences of the abuse of trusts*

The claimant (now appellant) sought leave to appeal and was successful. Before the appeal court she based her argument on two grounds:

> [F]irst that the *court a quo* had erred by not taking into account that the respondent (previously the plaintiff) enjoyed the benefit of occupying, farming and receiving income from the Jubileeskraal. Secondly, that the court found that the assets of the Jubilee

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297 *Badenhorst* Paras 259A-B and Harding *Importance of adhering to the basic trust idea* 24.
298 Paras 259H-I.
299 Paras 261A-B.
300 See ch 2.3 Control and alter ego.
301 Unreported judgement, case number 26600/98 TPD.
302 Paras 29-34.
303 *Badenhorst v Badenhorst* 2006 2 SA 255 (SCA).

> trust did not form part of the parties 'joint estate' and that the appellant was therefore not entitled to 50 percent thereof.

The Supreme Court of Appeal found that the court *a quo* erred by excluding the trust assets for the purpose of redistribution.[304] The court furthermore incorrectly approached the legal nature of a trust when it concluded that the trust was a separate legal entity. The court in its rejection of the judgement by the *a quo* court referred to the *MacNellie's Estate* case.[305] With reference to the issue of control, the court also noted that matters related to trustees and the founder were interpreted incorrectly.[306] The court further held where a party did not make a bequest or transferred assets with the intention of frustrating the claims of the divorcing spouse, the assets *in casu*, will not form part of the redistribution order. It was concluded by the court that:

> The present case is a classic instance of one party, the respondent in this case, having full control of the assets of the trust and using the trust as a vehicle for his business activities. A clear indication of this was found in the provisions of the trust deed.[307]

There was also evidence that the respondent was in full control, paying no attention to the separation of trust and personal assets, and were it not for the trust form, he would have had personal ownership of the assets. The Supreme Court of Appeal acknowledged that in *Jordaan* and *Grobbelaar* the courts resolved the cases by taking into account the value of trust assets when making a redistribution.

According to Stafford[308] the reason why the court *a quo* failed to come to the same conclusion as that of the Supreme Court of Appeal is their lack of knowledge with regard to the requirements and application of the sham and alter ego doctrines. He further wrote that it is not only the courts that confuse them, and he referred to Joffe[309], who also failed to correctly differentiate between **sham** trusts and **alter ego** trusts.

Joffe[310] was of the opinion that the trust was a sham for the primary reason that Mr Badenhorst were found to have *de facto* control over the trust assets. However, as founded in chapter 2.5, this is contrary to what the courts found true. *De facto* control

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304 262F-G: "In my view the value of the trust assets should have been added to the value of the respondent's estate. The decision of the trial Judge to exclude the trust assets amounted to a clear misdirection, enabling this court to substitute its discretion for that exercised by the court below."
305 *MacNellies Estate*.
306 Paras 260I-J.
307 Par 260D.
308 Stafford *The dangers of translocating Company Law principles into Trust Law* 48.
309 Joffe 2007 *De Rebus* 25.
310 Joffe 2007 *De Rebus* 25.

can be seen as being synonymous to the alter ego, because a valid trust was created, but the trustee was abusing his power of control. A trust is only found to be a sham when no valid trust was formed and one of the essential requirements was not met. Harding[311] correctly states that nowhere in the facts before the court, the lack of an essential requirement was present. The *Badenhorst* case is a good example of a person abusing his control as founder or trustee, resulting in the trust becoming his alter ego. The Supreme Court of Appeal confirmed this position. The instance where a court finds a trust to be the alter ego of a person and orders the value of the assets in the trust to form part of the redistribution order, is referred to as piercing the veil. Even though the Supreme Court of Appeal did not refer to the process of removing the trust protection, or including the value of the assets as piercing the veil, this is the legal name for this engagement. Harding[312] concluded by saying what was already confirmed in the case:

> It follows then that abuse of the trust form, by not adhering to the basic trust idea in the administration of the trust in this case led to the inclusion of the value of the trust assets in the personal estate of the trustee upon divorce.

Badenhorst was one of the first divorce cases relating to trusts. This case was also important for the fact that it determined that the control a trustee has over the trust assets have to be *de facto* and not necessarily *de iure*. This case also introduced matrimonial proceedings to trust law in a sense. Given that a wife cannot 'expect a meal ticket for life' when asking maintenance in a redistribution order, she is still entitled to share in the growth of the joint estate in the ratio that she contributed to the growth. Thus, piercing the veil of a trust that frustrated a spouse's claim, is in the author's opinion just and fair. What would be interesting to know is what SARS' position is with regard to cases where the court pierces the veil and orders the value of the trust assets to be added to the estate of the abuser. In terms of section 3(3)(d) of the Estate Duty Act, all the property in the estate of the deceased, prior to his death, must be included as property in his estate when calculating the estate duty payable.

The following case makes it apparent that the court will give effect to the true state of affairs, substance over form, as mentioned earlier. The type of control, enjoyment and way the trust is administered are all factors that the court take into consideration. The court found in *Jordaan* that his intention with the trust was to derive a benefit for himself.

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311 Harding *Importance of adhering to the basic trust idea* 27.
312 Harding *Importance of adhering to the basic trust idea* 27.

5.2 Jordaan v Jordaan

5.2.1 Facts[313]

Mr Jordaan, a wealthy business man who created several trusts during his business activities, was married out of community of property to Mrs Jordaan. In Mrs Jordaan's application for divorce she requested that the assets of the respective trusts be taken into account by the courts when making a redistribution in terms of section 7(3) of the *Divorce Act*.[314] She argued that the trusts were only a mechanism to hide his personal assets. There were five trusts involved namely, *Jopsama trust*, the *Groothoek trust*, *JJ Jordaan trust*, *JJ Jordaan Investment trust* and the *Jomar trust*.

5.2.2 Judgement

Traverso summarised the *Jordaan* case after contemplating how the trustees administered the trusts, and found the following:[315]

1. The way in which the trusts were administered in the past is an important factor in the determination of a redistribution order under Section 7 (3).[316]

2. It was clear from undisputed evidence and financial statements relating to the various trusts involved that vast amounts of money moved between trusts without any formal decision authorising it, Mr Jordaan made the transfers as he deemed fit.[317]

3. Loans were made to Mr and Mrs Jordaan's children without any formal decision or record keeping to this effect.[318]

4. Evidence showed that Mr Jordaan had regarded trust income as his personal income.[319]

The defendant's own testimony proved to the court that he regarded the trust to be his alter ego, being an instrument from which he could benefit financially. It was clear that

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313 Paras 288F-G.
314 70 of 1979.
315 Van der Linde & Venter 2002 *De Jure* 355.
316 Harding *Importance of adhering to the basic trust idea* 22 and see *Jordaan* par 300E translated.
317 Harding *Importance of adhering to the basic trust idea* 22 and see *Jordaan* par 300E translated.
318 Par 300H: "Weereens is daar geen notules oor hierdie lenings goed te keur nie en dit is gemene saak dat daar geen werklike lenings aan die kinders gemaak is nie".
319 Harding *Importance of adhering to the basic trust idea* 22 and *Jordaan* paras 300I-J (translated).

the defendant had the intention to create the trust directly when his wife contemplated the divorce, merely to place the assets out of reach of the wife. The court concluded that it will be just and fair to include the value of the trust assets in the redistribution order. Mr Jordaan failed to adhere to the core idea of a trust, administering the trust without making a distinction between the enjoyment and control of the trust.[320]

5.3 Conclusion

In the last case the evidence was so compelling that the court did not even have to look into the circumstances of Mr Jordaan to justify piercing of the veil, it was the obvious conclusion. It seems that the courts approach trusts in the same way, whether they relate to divorce or insolvency matters. From all the cases discussed in the two chapters, it is clear that the court's main concern is adherence to the basic trust idea.[321] The courts would first determine whether a trust complies with all the trust essentials, forming a valid or invalid trust. From this determination the courts can conclude whether the trust *in casu* is a sham or an alter ego, and after this finding, they would continue to address the consequences. The presiding judge testified in *Van Zyl v Kaye* that to his remembrance, the court has not as yet pierced the veil in the true sense of the word. The closest it has come to doing so was in *Van der Merwe* case. He corrected most of the authors who thought that the veil was pierced in the *Badenhorst* case. He stated that the Badenhorst case was merely an equitable distribution of assets between spouses in terms of section 7(3) of the *Divorce Act*. The judge motioned that he might be wrong in his interpretation of the facts of the Badenhorst case, and if the trust were pierced, it was done on the premise of an *unconscionable* act to evade his obligations at the dissolution of the marriage, namely maintenance or equal division of the joint estate. The author is of the opinion that this act of Mr Badenhorst, and in turn of the court, is exactly what piercing of the veil entails. The protection of a trust form is removed and the value of the assets is taken into account for either the claims of creditors in insolvent cases and divorcing spouses in matrimonial cases.

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320 Paras 301C-E.

321 Meaning there must be separation between enjoyment and control of the trust assets.

6 Conclusion and recommendations

It is clear from the argument of this study that the core idea of a trust must be adhered to in order to avoid unfortunate and definite detrimental consequences. This core idea is ultimately the separation of control and enjoyment of trust assets by the trustees.[322]

Several questions related to trusts were addressed in an attempt to arrive at the answer of the overarching question. This overarching question probed the circumstances under which a court will go beyond the trust veil to make assets available for redistribution in insolvency and divorce matters.

The first focal point was the legal nature of a trust[323]. In this regard paragraph 2.2 concluded that when considering the independence of the trust entity, the separation between trust and personal estates, the comparison with a *fideicommissum* and the different types of trusts, a trust exists as a separate entity and that the estates of the trust and trustee must be kept separate at all times. A trust has no legal personality in general and under common law. There are only a few legislative provisions for which a trust would be regarded as a legal entity that enjoys independent standing. If estates are kept separate and the trust in question aims to benefit beneficiaries, the veil secures the protection of the assets in the trust as long as the situation and intention with the assets remains the same and *bona fide*.

Following the above, the focus shifted to the factors that assist the courts in determining whether a trust is valid and if the veil may be pierced. Stafford states: “a trust only secures absolute certainty when a court proclaims a trust to be valid”[324] The discussion highlighted the essentials of a trust, stating that a valid trust will only come into existence when all the requirements are met. The cases discussed reveal that the point of departure for the courts when dealing with a trust is first to determine whether all the essential requirements have been met. After this determination, they will go ahead to establish a sham, if all requirements were not met, and an alter ego, if abuse of a valid trust was evident. The factors that the courts emphasise are the *intention* of the founder when creating the trust, or the *intention* of the trustees in the way they administer and

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322 *Trust Act*.
323 Ch 1.2 (a) of this dissertation.
324 Stafford *The dangers of translocating Company Law principles into Trust Law* 181.

control the trust. *Control* specifically refers to how the trustees control the trust assets. Are they objectively transacting for the benefit of the beneficiaries, or are they seeking own benefit without separating their assets from the trust assets?

The dissertation also concentrated on the differentiation between a sham trust and an alter ego trust.[325] Upon examination of the case law, it became apparent that there are two possible scenarios that result from abuse of the trust form. The first example is a **sham** trust, where the founder never had the intention to form a trust, or some of the essential requirements of a trust are not met, resulting in no trust being formed.[326] Yet, the persons who know that no valid trust came into being still purport to outsiders that a valid trust has been established. The other possible scenario is where a trust is found to be the **alter ego** of a trustee.[327] This is the scenario that surfaces most of the instances in case law. The alter ego trust is a validly established trust that complies with all the essentials of a trust. However, over time the trustees' intention with the trust has changed or the control over the assets are no longer *bona fide* or separate from their personal assets.

The origin and development of the doctrine of piercing the veil as part of trust law was also examined in this mini-dissertation. The next question that required investigation was whether company law doctrine can be used by courts in the trust law sphere. There is criticism against the courts using a company law doctrine in trust law. However, it is the author's opinion that South Africa practises law differently from law systems found in other jurisdictions. Courts have the right and duty to develop common law and interpret legislation as long it is in line with the *Constitution*. Therefore, it is possible to use the said doctrine in South Africa as it is currently entertained in most case law. This practise serves the demands trust law currently has. Luckily, the doctrine is well-established and accepted in company law, and the only hurdle is to adopt and extend this doctrine into trust law.

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325 See ch 2.5 of this mini-dissertation.

326 *Khabola* case, unreported judgement [2011] ZASCA 34 of 28/03/2011.

327 *Jordaan*, *Badenhorst*; *Parker*, *Thorpe*; *Van der Merwe*, *First National Bank v Britz* 2011 ZAGPPHC 119 of 20/07/2011 and *Rees v Harris*.

The last aspect that received attention is the consequences for a trustee when the trust veil is pierced. Harding[328] states the following in this regards:

> Adherence to the basic trust idea would have precluded the said consequences for the parties involved in the trust.

This was the conclusion derived from all the cases discussed. Chapters 4 and 5 showed that when a court pierces the trust veil, negative consequences follow for the trustees of the trust. They face the risk of the removal of the protection of trust assets from claimants such as creditors and divorcing spouses with redistribution orders. As a result the founder/trustee can be held personally liable. In cases of insolvency where a trustee was personally liable for debt, but is declared insolvent, the court may, if they find that the trust was used as a protection mechanism to frustrate the claims of the trustee's creditors, pierce the trust veil. This will result in the court allowing that the assets specifically hidden from the creditors be regarded as the trustee's personal assets, and creditors may lay claim on it. With reference to divorce cases, if a trust is found to be a spouse's alter ego, the divorcing spouse will be granted a redistribution order by a court. This order will include the value of the trust assets as personal property of that trustee spouse, although the assets will remain in the trust. The trustee spouse will be ordered to pay over the value thereof as ordered by the court. This might result in the trustee spouse actually feeling the punishment and not merely paying over some assets and having less in the trust.[329] Adding the assets from the trust to the trustees' personal estate would obviously also have estate duty consequences.[330]

From the case law it became evident that the courts view piercing the trust veil as a last resort.[331] The courts will not pierce the veil if there is another remedy[332] that is just and equitable and can be successfully employed to administer justice between the parties.

In the author's opinion, when piercing of the trust veil is chosen as a remedy for a trust that was abused, some sort of personal liability of the founder/trustee must be ordered by the court, for example a delictual remedy for loss or compensation for damages. It is

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328 Harding *Importance of adhering to the basic trust idea* 53.

329 This is also one of the concerns that was raised in ch 2. Is the trustee now left with an amount to pay to his wife and the assets left untouched in the trust? Nothing stops him from continuing with the abuse.

330 *Jordaan* and *Badenhorst*.

331 Stafford *The dangers of translocating Company Law principles into Trust Law* 129.

332 *Kay v Van Zyl* par457D.

suggested that the court considers adopting this doctrine formally as legislation to ensure legal certainty for persons who use trusts or deal with trusts. A perfect example or blue print for this adoption is section 20(9) and section 218 of the *Companies Act*.

After detailed consideration of all the aspects in this research, one aspect remains unanswered. Legal certainty is key to any transaction, and piercing of the corporate veil is clearly directed by the common law, which is supplemented by the new provisions in the *Companies Act*. Piercing the trust veil is to some extent also settled and the case law discussed seems to repeat itself in procedure and requirements, restoring some certainty that had been lost. An aspect that cannot be answered affirmatively is what happens in the case where the court finds a trust to be a sham. It is known that no valid trust has been established, but what will the effect be on transactions that had been concluded with and by the trust with third parties, and who will be the legal owners of the assets in the ‘invalid trust’?.

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