

6 NOVEMBER 2019


DISPUTE RESOLUTION ALERT

IN THIS ISSUE >

Are sureties still liable for a debt if the original causa is based on an invalid contract?

The Constitutional Court dealt with this question in *Shabangu v Land and Agricultural Development Bank of South Africa & Others* [2019] ZACC 42. The applicant and others stood as sureties for a loan agreement entered into between the Land and Agricultural Development Bank of South Africa (Land Bank) and Westside Trading 570 (Pty) Ltd (Westside) for the development of urban property.

FOR MORE INSIGHT INTO OUR
EXPERTISE AND SERVICES

CLICK HERE 



CLIFFE DEKKER HOFMEYR

Are sureties still liable for a debt if the original causa is based on an invalid contract?

They argued that the liability in the acknowledgment of debt was based on the liability of Westside under the invalid loan agreement. Consequently, the acknowledgment of debt was tainted by the self-same invalidity.

The Constitutional Court dealt with this question in *Shabangu v Land and Agricultural Development Bank of South Africa & Others* [2019] ZACC 42. The applicant and others stood as sureties for a loan agreement entered into between the Land and Agricultural Development Bank of South Africa (Land Bank) and Westside Trading 570 (Pty) Ltd (Westside) for the development of urban property.

Subsequently it came to light that the loan agreement was invalid and therefore *void ab initio* as the transaction underlying the loan was beyond the scope of the Land Bank's statutory powers in terms of the Land and Agricultural Development Bank Act 15 of 2002.

By this time, however, funds had already been advanced by the Land Bank to Westside. Including interest, Westside was indebted to the Land Bank in the amount of R95 million. The financial director of Westside then signed an acknowledgement of debt in which Westside accepted liability to repay R82 million in full and final settlement of its indebtedness.

Westside then defaulted on its payments. The Land Bank then instituted proceedings against Westside and the sureties. Subsequent to the institution of proceedings, Westside was liquidated. The Land Bank therefore dropped its claim against Westside and pursued only the sureties.

It was common cause between the parties that the original loan agreement was invalid. The sureties had limited their liability specifically to Westside's obligations under the loan agreement. They argued that the liability in the acknowledgment of debt was based on the liability of Westside under the invalid

loan agreement. Consequently, the acknowledgment of debt was tainted by the self-same invalidity. Following this they argued that they could not be held liable when their accessory obligation related to an invalid contract.

After their application for leave to appeal to the Supreme Court of Appeal was unsuccessful, the Applicant sought and was granted leave to appeal to the Constitution Court.

In the court *a quo*, the Land Bank had been successful by relying on the judgment in *Panamo Properties 103 (Pty) Ltd v Land and Agricultural Development Bank of South Africa* [2015] ZASCA 70. *Panamo* held that it did not necessarily follow that because a principal agreement was invalid, that the ancillary agreement was also invalid. *Panamo* was, however, in the context of a mortgage bond as security and not suretyships. *In casu*, the court *a quo* held that the acknowledgment of debt was properly proved, and that the debt to which it referred was properly covered by the suretyships.

The Constitutional Court held that the *Shabangu* matter was distinguishable from *Panamo* on the basis that the mortgage bond in *Panamo* itself stipulated that a bond would be passed to cover "*in general ... any existing or future debt that Panamo owes or may owe to the [Land] Bank*". The bond was therefore wide enough to provide for any other liability which could or would be incurred by the debtors.

The Constitutional Court found that on the facts of *Shabangu* there was no scope for arguing that there was a transformation of the nature of the debt into something new and valid (for example an enrichment claim).

Are sureties still liable for a debt if the original causa is based on an invalid contract?...*continued*

One should therefore be very careful to ensure that an acknowledgment of debt is not in itself tainted by invalidity, and be alive to the extent to which suretyships are limited.

The Constitutional Court therefore found that the acknowledgment of debt could not be premised on, or have as its *causa*, the invalid loan agreement. This would only perpetuate the invalidity of the indebtedness and tainted the acknowledgment of debt, making it too invalid. The court therefore found that the sureties could not be held liable where the debt underlying their accessory obligation was based on an invalid contract.

The Constitutional Court did find that it was possible that the subsequent agreement, that is, the acknowledgment of debt, could be valid if the original invalidity was overcome in one way or another. This was not done.

It was suggested that this original invalidity could have been overcome in the acknowledgement of debt by governing the recovery of what was transferred under an invalid agreement in terms of a claim for unjustified enrichment.

Unjustified enrichment occurs where a legal entity receives a benefit or value from another at the expense of the latter without any legal cause for such receipt or retention of the value or benefit by the former.

Therefore, if the acknowledgement of debt is based on a claim for unjustified enrichment then it would be valid, and the sureties, depending on the wording of the suretyship agreement, could be held liable.

In this matter, however, such alternative framing of the creditor's claim in the acknowledgement of debt would alone not have saved their claim in respect of the sureties. The wording of the surety agreements only bound the sureties for the "indebtedness" which flowed from the original (invalid) agreement, so a valid acknowledgement of debt based on enrichment alone would not have led to claims against the sureties either.

In summary, the outcome of this case would have been different if the acknowledgement of debt stated as the cause of the indebtedness the unjustified enrichment of Westside (and by means of ancillary liability – the sureties), and if the suretyship agreements signed were wide enough to incur liability for the sureties for any indebtedness by the principal debtor to the creditor as opposed to limiting the liability of the sureties to the indebtedness arising directly out of the loan agreement. One should therefore be very careful to ensure that an acknowledgment of debt is not in itself tainted by invalidity, and be alive to the extent to which suretyships are limited.

*Andrew MacPherson and
Belinda Scriba*

CDH is a Level 1 BEE contributor – our clients will benefit by virtue of the recognition of 135% of their legal services spend with our firm for purposes of their own BEE scorecards.

CHAMBERS GLOBAL 2017 - 2019 ranked our Dispute Resolution practice in Band 1: Dispute Resolution.

CHAMBERS GLOBAL 2019 ranked our Public Law sector in Band 2: Public Law.

CHAMBERS GLOBAL 2018 - 2019 named our Corporate Investigations sector as a Recognised Practitioner.

CHAMBERS GLOBAL 2018 - 2019 ranked our Dispute Resolution practice in Band 2: Insurance.

CHAMBERS GLOBAL 2018 - 2019 ranked our Dispute Resolution practice in Band 2: Media & Broadcasting.

CHAMBERS GLOBAL 2017 - 2019 ranked our Dispute Resolution practice in Band 2: Restructuring/Insolvency.

Tim Fletcher ranked by CHAMBERS GLOBAL 2019 in Band 3: Dispute Resolution.

Lionel Egypt ranked by CHAMBERS GLOBAL 2019 in Band 2: Public Law.

Julian Jones ranked by CHAMBERS GLOBAL 2017 - 2019 in Band 3: Restructuring/Insolvency.

Pieter Conradie ranked by CHAMBERS GLOBAL 2019 as Senior Statespeople: Dispute Resolution.

Jonathan Witts-Hewinson ranked by CHAMBERS GLOBAL 2017 - 2019 in Band 2: Dispute Resolution.

Joe Whittle ranked by CHAMBERS GLOBAL 2016 - 2019 in Band 4: Construction.



CDH HAS BECOME THE EXCLUSIVE MEMBER FIRM IN AFRICA FOR THE:

Insuralex Global Insurance Lawyers Group
(the world's leading insurance and reinsurance law firm network).

[CLICK HERE TO READ MORE](#)



BAND 2
Restructuring/Insolvency

Cliffe Dekker Hofmeyr

RECOGNISED PRACTITIONER
Corporate Investigations

Cliffe Dekker Hofmeyr

EMEA
2017-2019
Recommended us in

TIER 1
Dispute Resolution

1ST BY M&A DEAL FLOW FOR THE 10TH YEAR IN A ROW.

2018 1st by M&A Deal Flow.
1st by M&A Deal Value.
2nd by General Corporate Finance Deal Flow.
1st by BEF M&A Deal Value.
2nd by BEF M&A Deal Flow.
Lead legal advisers on the Private Equity Deal of the Year.

BAND 1
Dispute Resolution

Cliffe Dekker Hofmeyr

BAND 2
Public Law

Cliffe Dekker Hofmeyr

BAND 2
Media & Broadcasting

Cliffe Dekker Hofmeyr

BAND 2
Insurance

Cliffe Dekker Hofmeyr

OUR TEAM

For more information about our Dispute Resolution practice and services, please contact:



Tim Fletcher
National Practice Head
Director
T +27 (0)11 562 1061
E tim.fletcher@cdhlegal.com



Thabile Fuhrmann
Chairperson
Director
T +27 (0)11 562 1331
E thabile.fuhrmann@cdhlegal.com

Timothy Baker
Director
T +27 (0)21 481 6308
E timothy.baker@cdhlegal.com

Eugene Bester
Director
T +27 (0)11 562 1173
E eugene.bester@cdhlegal.com

Lionel Egypt
Director
T +27 (0)21 481 6400
E lionel.egypt@cdhlegal.com

Jackwell Feris
Director
T +27 (0)11 562 1825
E jackwell.feris@cdhlegal.com

Anja Hofmeyr
Director
T +27 (0)11 562 1129
E anja.hofmeyr@cdhlegal.com

Julian Jones
Director
T +27 (0)11 562 1189
E julian.jones@cdhlegal.com

Tobie Jordaan
Director
T +27 (0)11 562 1356
E tobie.jordaan@cdhlegal.com

Corné Lewis
Director
T +27 (0)11 562 1042
E corne.lewis@cdhlegal.com

Richard Marcus
Director
T +27 (0)21 481 6396
E richard.marcus@cdhlegal.com

Burton Meyer
Director
T +27 (0)11 562 1056
E burton.meyer@cdhlegal.com

Zaakir Mohamed
Director
T +27 (0)11 562 1094
E zaakir.mohamed@cdhlegal.com

Rishaban Moodley
Director
T +27 (0)11 562 1666
E rishaban.moodley@cdhlegal.com

Mongezi Mpahlwa
Director
T +27 (0)11 562 1476
E mongezi.mpahlwa@cdhlegal.com

Kgosi Nkaiseng
Director
T +27 (0)11 562 1864
E kgosi.nkaiseng@cdhlegal.com

Byron O'Connor
Director
T +27 (0)11 562 1140
E byron.oconnor@cdhlegal.com

Ashley Pillay
Director
T +27 (0)21 481 6348
E ashley.pillay@cdhlegal.com

Lucinde Rhoodie
Director
T +27 (0)21 405 6080
E lucinde.rhodie@cdhlegal.com

Belinda Scriba
Director
T +27 (0)21 405 6139
E belinda.scriba@cdhlegal.com

Tim Smit
Director
T +27 (0)11 562 1085
E tim.smit@cdhlegal.com

Willie van Wyk
Director
T +27 (0)11 562 1057
E willie.vanwyk@cdhlegal.com

Joe Whittle
Director
T +27 (0)11 562 1138
E joe.whittle@cdhlegal.com

Roy Barendse
Executive Consultant
T +27 (0)21 405 6177
E roy.barendse@cdhlegal.com

Pieter Conradie
Executive Consultant
T +27 (0)11 562 1071
E pieter.conradie@cdhlegal.com

Willem Janse van Rensburg
Executive Consultant
T +27 (0)11 562 1110
E willem.jansevanrensburg@cdhlegal.com

Nick Muller
Executive Consultant
T +27 (0)21 481 6385
E nick.muller@cdhlegal.com

Jonathan Witts-Hewinson
Executive Consultant
T +27 (0)11 562 1146
E witts@cdhlegal.com

BBBEE STATUS: LEVEL ONE CONTRIBUTOR

Cliffe Dekker Hofmeyr is very pleased to have achieved a Level 1 BBBEE verification under the new BBBEE Codes of Good Practice. Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

This information is published for general information purposes and is not intended to constitute legal advice. Specialist legal advice should always be sought in relation to any particular situation. Cliffe Dekker Hofmeyr will accept no responsibility for any actions taken or not taken on the basis of this publication.

JOHANNESBURG

1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa. Dx 154 Randburg and Dx 42 Johannesburg.
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E jhb@cdhlegal.com

CAPE TOWN

11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E ctn@cdhlegal.com

STELLENBOSCH

14 Louw Street, Stellenbosch Central, Stellenbosch, 7600.
T +27 (0)21 481 6400 E cdh Stellenbosch@cdhlegal.com

©2019 8454/NOV

