

REAL ESTATE AND DISPUTE RESOLUTION ALERT

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CAN A MORTGAGE BOND SECURE A CLAIM FOR ENRICHMENT WHERE THE UNDERLYING LOAN AGREEMENT IS INVALID?

The facts of the *Panamo Properties 103 (Pty) Ltd v Land and Agricultural Development Bank of South Africa 2016 (1) SA 202 (SCA)* are, at first, quite run-of-the-mill: Land and Agricultural Development Bank (Bank) entered into a loan agreement with Panamo Properties 103 (Pty) Ltd (Panamo).

CAN A MORTGAGE BOND SECURE A CLAIM FOR ENRICHMENT WHERE THE UNDERLYING LOAN AGREEMENT IS INVALID?

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The facts of the *Panamo Properties 103 (Pty) Ltd v Land and Agricultural Development Bank of South Africa 2016 (1) SA 202 (SCA)* are, at first, quite run-of-the-mill: Land and Agricultural Development Bank (Bank) entered into a loan agreement with Panamo Properties 103 (Pty) Ltd (Panamo).

As security for this debt, the parties registered a mortgage bond. The matter took a more complicated turn when the Bank argued that the loan agreement was invalid due to its failure to comply with certain legislation. The Gauteng Local Division of the High Court was tasked with answering two main points of contention: Was the loan agreement invalid? If so, could the mortgage bond still be enforced, thereby allowing the Bank to claim back the money it lent to Panamo?

The High Court found in favour of the Bank. It declared the loan agreement to be invalid but decided that the mortgage bond could nevertheless be enforced. As the Bank had advanced money to Panamo under an invalid agreement, the Bank had a claim for enrichment. The court allowed this claim. This decision was confirmed by the Supreme Court of Appeal (SCA). How the SCA came to this conclusion and why is set out below.

Was the loan agreement invalid?

The SCA found that the loan agreement was invalid due to the Bank's failure to comply with certain provisions of the Land and Agricultural Development Bank Act, No 15 of 2002 and the Public Finance Management Act, No 1 of 1999.

Could the mortgage bond act as security for obligations other than those that arose from the loan, specifically?

A mortgage bond is always accessory to an obligation (in this case, the loan agreement). As a general rule, if the original obligation is unenforceable, the security in respect of it is unenforceable too. It is, however, not necessary that a principal obligation exists before a mortgage bond is entered into; a mortgage bond may be given as security for a *future* debt or as a continuing covering bond (such bonds may provide continuing covering security for all debts that may arise now or in future). Importantly, the *Panamo* case involved such a continuing covering bond. As stated by the court, the bond may therefore afford security for more than obligations arising under the loan. It is not necessarily extinguished merely because the loan is void, however this depends on the specific terms drafted into the bond.

Is the enrichment claim a valid obligation under the mortgage bond?

Although a principal obligation does not have to exist before a mortgage bond is entered into, there does have to be a valid (existing) obligation at the time enforcement of the mortgage

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The SCA confirmed the decision of the court a quo, deciding that the Bank's enrichment claim was secured by the mortgage bond despite the invalidity of the loan agreement.



bond is sought. The court pointed out that an enrichment claim gives rise to indebtedness, and there is no reason why a mortgage bond cannot secure a debt arising from an enrichment claim. Whether or not the *particular* mortgage bond could secure this kind of debt was a separate matter that had to be answered with reference to the bond's specific terms.

Could the particular mortgage bond secure the Bank's enrichment claim?

The SCA considered the preamble and certain clauses in the mortgage bond which were stated in broad terms. The bond was worded so as not to restrict it to cover indebtedness arising from the loan agreement alone. For example, clause 2.1 of the mortgage bond agreement afforded, among other things, continuing covering security, in general, for any existing or future debt that Panamo owed or may owe to the Bank. This clause reflected the position in the bond's preamble, which described the indebtedness in the broadest possible terms: liability to the Bank "for whatsoever reason".

The SCA then considered whether any clauses in the bond agreement specifically excluded a claim based on enrichment. In what followed, the SCA analysed various provisions of the bond agreement. Holistically, the SCA found that there was no basis for limiting the broad, all-encompassing language of the mortgage bond. Thus the SCA confirmed the decision of the court a quo, deciding that the Bank's enrichment claim was secured by the mortgage bond despite the invalidity of the loan agreement.

Conclusion

Although the SCA stated that the bond in this matter was "not a model of clarity", what the mortgagee did achieve was the creation of a covering bond with a wide enough net to catch a range of debts owed to the Bank including an enrichment claim against Panamo. This all-encompassing language was the reason the Bank could enforce its claim despite the invalidity of the loan agreement. It is thus important for mortgagees to make sure their mortgage bonds are drafted in a way that does not limit their security.

Emily West, Vincent Manko and Muhammad Gattoo

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