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CORPORATE & COMMERCIAL **ALERT**

IN THIS **ISSUE**

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Lease renewal clauses: Landlords and tenants beware

The tenant validly exercised the option during the initial term and the lease was renewed for a further five-year term.

The drafting of renewal clauses in leases continue to cause problems for landlords and tenants.

Such a clause was again the subject matter of a recent case in the Supreme Court of Appeal (SCA), *Shepherd Real Estate Investments (Pty) Ltd v Roux Le Roux Motors CC* (1318/2018) [2019] ZASCA 178 (2 December 2019).

The facts of the case were that the parties had entered into a lease in relation to petrol station premises in Paarl. The lease started on 1 December 2007 and was to endure for an initial term of five years, with a renewal period of "5 plus 5 years". The rental at commencement was R18,000 per month, escalating at 8% per year over the initial term.

As to the clause dealing with the determination of the terms that would apply on renewal of the lease agreement, it is worthwhile quoting the relevant text as provisions along the same lines are contained in many leases:

> "[The] renewal for the second lease renewal period, shall be on terms and conditions in compliance with the Landlord's then standard letting policy, except that there shall be no right of further renewal and that the rental and costs shall be mutually agreed upon in writing between the Landlord and the Tenant when the right of renewal is exercised."

The lease also contained an arbitration clause.

The tenant validly exercised the option during the initial term and the lease was renewed for a further five-year term.

However, when the tenant tried to exercise the second option to renew for a third five-year term, the landlord said that it was amenable to the proposed renewal at an agreed rental of R150,000 per month, plus value-added tax. In response, the tenant contended that a fair rental was an 8% per year escalation on the then prevailing rental. The tenant also proposed that the matter be referred to arbitration. The landlord rejected that contention and that proposal, and proceeded with an application to evict the tenant as it considered the lease to have expired due to the effluxion of time.

The landlord argued that the rental amount for the renewal period was neither determined nor determinable; that the relevant provision of the renewal clause was "an agreement to agree" and, accordingly, was void for vagueness; and that there was no obligation on the parties to negotiate in good faith or to reach an agreement on a rental amount that is objectively reasonable.

The tenant argued that the renewal provision did not reflect the intention of the parties and that the provision should be rectified to reflect the correct intention

Lease renewal clauses: Landlords and tenants beware

...continued

The High Court dismissed the landlord's application. The landlord appealed to the SCA. The SCA ruled in favour of the landlord and upheld the appeal.

or, alternatively, that there was a tacit term in the lease agreement that the rental would be reasonable rental which could be established and determined objectively. The tenant also contended that the parties had agreed to arbitration.

The High Court dismissed the landlord's application. The landlord appealed to the SCA. The SCA ruled in favour of the landlord and upheld the appeal.

Judge Ponnan considered the essential legal propositions in cases such as these on the basis of the judgments in South African, English and Australian court cases.

The Judge concluded as follows at pages 11 and 12 of the ruling:

> "[A]lthough the position in relation to 'agreements to negotiate in good faith' remains a complex one in Australia in the light of *Coal Cliff Collieries*, courts there, like other comparable jurisdictions, will not enforce 'an agreement to agree'. That accords as well with the position in our law."

(Footnote omitted.)

Judge Ponnan proceeded as follows at page 12 of his judgment:

> The proper approach in an enquiry such as the present depends upon the construction of the particular agreement. Accordingly, it becomes necessary to analyse the relevant paragraph to decide whether its proper characterisation is merely an agreement to agree or whether it contained legally enforceable obligations.

The court essentially held (at page 13) that the renewal clause was too "illusory or too vague and uncertain to be enforceable ".

As to the notion that the matter should have been referred to an arbitrator, the court found that an arbitrator "could not give effect to arrangements that the parties themselves had not concluded and then require the party, who is resisting, to continue with the ongoing relationship". The court also held that, as the lease agreement had terminated by effluxion of time, the tenant could in any event no longer invoke the arbitration clause.

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What the judgment highlights is that it is absolutely critical that renewal clauses in leases be drafted with great care.

The court made short shrift of the tenant's arguments for the rectification of the provisions or the introduction of a tacit term. As to the former, the judge found that the tenant's obligations were far-fetched or untenable, and, essentially, that the tenant had only itself to blame for signing an unfavourable contract. As to the introduction of a tacit term, it was essentially held that the parties had applied their minds to the lease agreement and had expressly agreed on the terms of the renewal clause, and that, accordingly, there was no scope for introducing a tacit term.

What the judgment highlights is that it is absolutely critical that renewal clauses in leases be drafted with great care. The parties must either provide for an agreed and fixed amount of rental that will apply on renewal or, alternatively, if they do leave the rental to be determined at the time of the renewal, they should provide for a deadlock-breaking mechanism.

For example, in the alternative arrangement, the parties could include a provision along the following lines:

> "The monthly rental payable during the renewal period shall be a market-related rental escalating at a market-related rate as agreed in writing between the parties, failing which agreement, the rental and rate determined by an independent expert who shall be appointed by written agreement between the parties and, failing which agreement, by [some determined qualified person, eg a named registered valuer]. The independent expert shall act as an expert and not as an arbitrator, and his or her decision shall be final and binding on the parties.
>
> If the rental and rate has not been determined by the start of the renewal period then the following rental shall be paid until such time as the new rental and rate has been finally determined, when suitable adjustments in rental shall be made with retrospective effect: The rental payable in respect of the month immediately prior to the termination date escalated by [X]% and thereafter escalating annually on each anniversary of the start date of the renewal period at a rate of [X]% per year."

Ben Strauss

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Should regulated companies approach the TRP for share buy-backs of more than 5%?

In other words, does section 48(8)(b) introduce an eighth *"affected transaction"* which falls within the TRP's jurisdiction?

There is often debate as to whether share repurchases of more than 5% by a regulated company fall within the jurisdiction of the Takeover Regulation Panel (TRP).

Briefly put, the TRP regulates *"affected transactions"* that involve regulated companies and must provide its approval before implementation of such transactions. Section 117(1)(c) of the Companies Act 71 of 2008 (Companies Act) lists seven *"affected transactions"* and one of the affected transactions is a scheme of arrangement between a regulated company and its shareholders as contemplated in section 114 (section 117(1)(c)(iii)). Section 115 sets out the procedural requirements applicable to fundamental transactions, including a section 114 scheme of arrangement.

In terms of section 48(8)(b) of the Companies Act, if a company repurchases more than 5% of a class of its shares in a single transaction or an integrated series of transactions, such repurchase is *"subject to the requirements of sections 114 and 115"*. Since a section 114 scheme of arrangement undertaken by a regulated company constitutes an *"affected transaction"* within the TRP's jurisdiction and section 115 deals with the required approvals, the question that arises is whether, by subjecting a share buy back of more than 5% to the requirements of sections 114 and 115, a section 48(8)(b) buy-back by a regulated company must be treated as an *"affected transaction"* where the TRP is required to provide its prior approval under section 121 of the Companies Act. In other words, does section 48(8)(b) introduce an eighth *"affected transaction"* which falls within the TRP's jurisdiction?

In our view, the correct interpretation is that a share buy-back in terms of section 48(8)(b) should not become a scheme of arrangement by virtue of the section imposing the requirements of sections 114 and 115 onto a company that repurchases more than 5% of its shares. It is submitted that a company repurchasing its shares by means of a scheme of arrangement as envisioned by section 114(1)(e) is fundamentally different from a share repurchase in terms of section 48(8)(b).

Under section 114 of the Companies Act, the board of the company can propose a scheme of arrangement between the company and its shareholders (or any of them) for the repurchase of their shareholding (or a specified portion). In this instance, if the requisite 75% approval is obtained and other statutory requirements have been complied with, the scheme of arrangement is binding on the shareholders who are parties to such arrangement by operation of law, irrespective of whether or not such shareholders voted in favour of the arrangement. Where the scheme of arrangement being proposed, for example, involves a compulsory repurchase of a specified percentage of all shareholders' shareholding in the company at a stated repurchase price, all shareholders will, if the scheme becomes operative, have the relevant portions of their shareholdings expropriated.

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Should regulated companies approach the TRP for share buy-backs of more than 5%?*...continued*

From a legal perspective it is not clear whether or not the TRP has jurisdiction over share buy-backs of more than 5% undertaken by regulated companies.

Where a company proposed to repurchase more than 5% of any class of its shares by mutual agreement, shareholders are not bound by the terms of any arrangement to sell their shares, and receive a specified repurchase consideration, unless they agree to doing so – no majority vote legally binds the minority. A repurchase by agreement therefore does not have the same characteristics nor legal effect as a repurchase by way of a scheme of arrangement.

It is argued that a regulated company can choose to implement a share repurchase in terms of section 48(8)(b) or by means of a section 114 scheme of arrangement. If a regulated company uses a scheme of arrangement to give effect to a share repurchase, such acquisition will constitute an *"affected transaction"*, for which the TRP's sign off must be obtained.

Where a company repurchases more than 5% of any class of its shares by agreement with one or more selling shareholders, our opinion is that the correct interpretation is that such repurchases do not amount to a scheme of arrangement, and the regulated company should only have to comply with the procedural requirements of sections 114 and 115. Past practices of the TRP have however shown that the TRP's view is that section 48(8)(b) share buy backs do fall within the TRP's jurisdiction and that the TRP does require regulated companies to comply with the Takeover Regulations, and obtain the TRP's approval, prior to implementation of such repurchases.

From a legal perspective it is not clear whether or not the TRP has jurisdiction over share buy-backs of more than 5% undertaken by regulated companies. In fact, former Executive Director of the TRP, Madimetja A L Phakeng concedes to this legal uncertainty in respect of section 48(8)(b) in his dissertation of April 2019 where he states that –

> *"The Companies Act of 2008 however, is not specific whether or not such a repurchase '...now becomes an arrangement as contemplated in section 114.' The legislature must make it clear that these transactions are not affected transactions. This is important particularly when one considers the numerous and cumbersome obligations relating to the concept of an affected transaction."*

Despite this legal uncertainty, regulated companies should be aware of the TRP's past practices of regulating section 48(8)(b) share buy-backs. There is therefore no guarantee that a regulated company repurchasing more than 5% of its shares will be in the clear with the TRP if it only complies with the requirements of sections 114 and 115. There is a risk that the TRP requires section 48(8)(b) buy-backs to be approved or exempted by the TRP, even though the legal basis upon which the TRP has such jurisdiction is admittedly unclear.

Johan Green and Yusrah Ehrenreich

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The Property Practitioners Act: What is it all about?

In order to achieve its objects, the Act uses the phrase "property practitioner" which is much broader than an "estate agent" under the EAA Act.

The President has recently signed into the law the Property Practitioners Act 22 of 2019 (Act). The date of commencement of the Act is still to be determined. However, those in the property industry ought to start getting to grips with the provisions of the Act as soon as possible.

The Act has repealed the Estate Agency Affairs Act 112 of 1976 (EAA Act) in its entirety. It did so to achieve three primary objects:

(1) to address the slow transformation in the property sector;

(2) to integrate and consolidate all role-players within the property sector under one umbrella statute; and

(3) to address the deficiencies in what has been a largely ineffective system of monitoring estate agency matters and protecting consumers and their trust funds.

Who is a "Property Practitioner"?

In order to achieve its objects, the Act uses the phrase "*property practitioner*" which is much broader than an "estate agent" under the EAA Act. A property practitioner is any person who, for the acquisition of gain, directly or indirectly, on the instructions or on behalf of another:

1. sells, purchases, manages or publicly exhibits for sale any property or business undertaking;
2. leases or hires or publicly exhibits for hire any property or business undertaking;
3. collects or receives money payable for a lease;
4. provides, procures, facilitates, secures or otherwise obtains or markets financing for or in connection with the management, sale or lease of a property or business undertaking; and/or
5. renders services as an intermediary to effect the conclusion of an agreement to sell or let a property or business undertaking (except where this is not done in the ordinary course of the person's business; where it is done by a natural person in their personal capacity, or where the person is an attorney, candidate attorney or sheriff).

Thus, the definition (and thus the application of the Act), extends well beyond estate agents. It notionally also includes auctioneers, property developers, property managers, franchisees, providers of bridging finance and bond brokers (aside from financial institutions) and, for purposes of certain provisions all directors, trustees, and/or employees of property practitioners.

Anyone who falls within the ambit of the definition of a "*property practitioner*" is required under the Act to obtain a certificate issued by the Fidelity Fund on an annual basis. Without a valid certificate, a property practitioner may not render services or receive fees. In fact, conveyancers are prohibited from paying any money to a property practitioner without receiving a copy of that property practitioner's valid Fidelity Fund certificate.

The Property Practitioners Act: What is it all about?*...continued*

Any person convicted of an offence in terms of the Act is liable to pay a fine, or to imprisonment for up to 10 years.

The Fidelity Fund's primary purpose is to reimburse persons who suffer pecuniary loss by virtue of:

(1) theft of trust money by property practitioners; or

(2) failure by property practitioners to comply with the provisions of the Act requiring a separate trust account and proper accounting records.

Property practitioners are also required to maintain indemnity insurance (to the extent required by the Minister of Human Settlements); comply with a property practitioners' code of conduct (to be prescribed by the Minister of Human Settlements); and to provide certain mandatory disclosures to potential purchasers and lessees. These obligations are all designed in order to ensure that consumers are protected. Any property practitioner in contravention of the Act will be required to repay any fees received for a property transaction, and may be issued with a fine. Furthermore, any person convicted of an offence in terms of the Act is liable to pay a fine, or to imprisonment for up to 10 years.

The Property Practitioners Regulatory Authority

The Act has established the Property Practitioners Regulatory Authority (Authority). The intention is for the Authority to replace the Estate Agency Affairs Board. The Authority is required, among other things, to ensure compliance with the Act; to regulate the conduct of property practitioners; to implement measures to transform the property sector, and to conduct campaigns to educate property practitioners and consumers.

In terms of the Act the Authority is given far-reaching enforcement powers. It is entitled to appoint inspectors who are authorised to enter, inspect and search any property practitioner's business premises without notice (aside from private residences, for which a warrant is required), and to request any document from a property practitioner. In the event of a contravention of the Act, the Authority is entitled to issue a compliance notice and a fine to the relevant property practitioner.

It is also envisaged that the Authority serve a dispute resolution function, by receiving complaints against property practitioners, referring disputes for mediation and/or appointing independent adjudicators to adjudicate complaints.

To achieve its object of being a consumer-focused piece of legislation designed to protect consumers in the property industry, the Act obliges property practitioners to deliver a "disclosure form" to a seller/lessor before concluding a mandate, and to a purchaser/lessee before making an offer. The disclosure form must be signed by all parties and attached to the sale or lease agreement. If no disclosure form is signed and attached, the Act provides that the agreement must be interpreted as if no defects or deficiencies of the property were disclosed to the purchaser. The Act also provides that the relevant lease or sale agreement must be in the official South African language requested by the purchaser or lessee, and obliges the Authority to "*conduct campaigns to educate and inform the general public of their rights in respect of property transactions and property practitioners of their functions, duties and obligations*".

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The Property Practitioners Act: What is it all about?*...continued*

Although the Act does not stipulate the grounds for the granting of exemptions, it does provide certain relevant considerations.

The Act has as one of its objects the transformation of the property sector. The Authority is mandated in terms of the Act to implement and assess measures to progressively promote an inclusive and integrated property sector. It is required to establish a Property Sector Transformation Fund which applies to all property practitioners, which must be used by the Authority for transformation and empowerment programmes, including programmes to promote black-owned firms; to encourage the participation and work-readiness of historically disadvantaged persons in the property sector; and to promote consumer awareness of property transactions and business undertakings. The Act further provides that Government must use the services of property practitioners who comply with BBBEE and employment equity legislation.

Any person may apply to the Authority to be exempted from any provision of the Act, by submitting an explanation of the reasons for the application and any supporting documents. Although the Act does not stipulate the grounds for the granting of exemptions, it does provide certain relevant considerations. For example, the Authority may consider whether the granting of an exemption is likely to negatively impact the general public, competition in the property sector, consumers' rights or the objects of the Act.

Recommendation

The Act is significantly stricter and more far-reaching than its predecessor, the EAA Act. In light of the serious consequences of non-compliance with the Act, any person who may fall under the broad definition of "property practitioner" would be well-advised to seek guidance from a legal practitioner and ensure strict compliance with the provisions of the Act.

Justine Krige and Georgia Speechly

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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.

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