



Republic of South Africa

**IN THE HIGH COURT OF SOUTH AFRICA
(WESTERN CAPE DIVISION, CAPE TOWN)**

[REPORTABLE]

Case No: 5434/2011

In the matter between:

NEDBANK LIMITED

Plaintiff

(Registration No. 1951/000009/06)

and

**SPANNENBERG, COLIN PETER
SPANNENBERG, YOLINDA AGNES**

**First Defendant
Second Defendant**

JUDGMENT DELIVERED ON 3 APRIL 2014

HENNEY, J:

Introduction:

[1] The Plaintiff's claim against the Defendants is for payment of the sum of R1 596 587,27 plus interest thereon. In addition, the Plaintiff seeks an order declaring the Defendants immovable property (which is their home and place of residence) specifically executable and costs.

[2] The Plaintiff's claim as set out in the Particulars of Claim is based on the following:

- (a) A written loan agreement ("the second further bond agreement") concluded on 10 December 2007, as subsequently restructured ("the restructured agreement") on 23 June 2008, entered into between the Plaintiff and the Defendants.
- (b) The fact that the Defendants are in arrears with their monthly repayments due in terms of the said second further bond agreement.

[3] To this the Defendants raised in essence two defences namely that:

- (a) The underlying agreement, or scheme, which gave rise to the signing of the second further bond agreement (annexure A) was void as being in contravention of section 38 of the Companies Act 61 of 1973 ("the Companies Act") applicable at that time. Therefore the said agreement upon which Plaintiff sought to rely was unenforceable.
- (b) The second defence was that the credit advanced in terms of the third home loan agreement amounted to reckless credit as envisaged in terms of Section 80 of the National Credit Act 34 of 2005 (NCA).

[4] During the trial the evidence mainly focused on the defence in terms of the Companies Act.

[5] It emerged after having heard the evidence of the First Defendant that no case was made out by the Defendants in respect of the second defence. Mr Warner appearing on behalf of the Defendant conceded this, and in my view correctly so. This judgment will therefore only deal with the defences in terms of section 38.

[6] Background Facts

During September 2005 the First Defendant (who is, and was married in community of property to the Second Defendant) was employed as the branch manager of the Cape Town branch of Airoad Express ("the Company"). He had been so employed since about 2000. He was approached by the director and shareholder of Airoad Express, Mr Mentrup ("Mentrup"), to buy shares in terms of which he would acquire 25,1% shareholding in the company for an amount of R1 079 000,00.

[7] First Defendant who at that stage only earned R10 500,00 per month, was not able to afford to pay for the shares. He was informed by Mentrup that he had made arrangements with Bruce Potgieter ("Potgieter"), a business manager in the employ of the Plaintiff, who were the bankers of Airoad

Express, to facilitate a process whereby he (the First Defendant) would be able to purchase the shares.

[8] This process is set out in a document drafted by Potgieter. The purpose of the document that was drawn up by Potgieter and/or signed by the area credit manager of the Plaintiff, Mr L Nel, and recommended by the Area Credit Manager of the Plaintiff, G Gouws, was to review the financial position of Airoad Express. According to the document, it was also to approve a request of R1 079 000,00, a medium term loan for First Defendant who at that stage, was not a client of Nedbank.

[9] In the document titled "APPLICATION FOR FACILITIES" relating to the financial position of Airoad Express (page 9 document)¹, the Plaintiff's representative states under paragraph 2:

"We have been requested to provide medium term loan finance of R1, 079K in the name of K. Spannenberg² to enable the purchase of 25,1% shareholding in Airoad Express (Pty) Ltd".

Then further on the same page it is stated:

"C Spannenberg has been with Airoad Express (Pty) Ltd for the past five years and is employed as the Cape Town Branch Manager. The

¹ Page 23 – Trial Bundle.

² Should be C Spannenberg.

Board's turnover in 2000 amounted to R10K per month, which has grown to R140K per month. Currently"

[10] Then further ... *"Customers that have previously dealt with Airoad Express (Pty) Ltd [were] forced elsewhere as a result of non BEE compliance include Ellerines who has 500 stores nationally. Ellerines gave notice to Airoad Express (Pty) Ltd two years ago that they would channel their distribution elsewhere should they not be BEE compliant by February 2006."*

On page 10 of the report³ it is further stated by Potgieter:

"In support of the requested MTL⁴ we will be provided with R476K tangible security (variation agreement) that will be raised via available security in Spannenberg's Cape Town property.

The requested MTL to be paid over a five year period. Spannenberg's cost to company earnings will be increased to meet this monthly instalment (additional R22K per month). We will register a bond over Spannenberg's property but will only place reliance on this security at 80% of the valuation current outstanding back with ABSA amount to +- R110K."

³ Trial Bundle page 23(a).

⁴ Medium Term Loan.

[11] Then on page 11⁵ Potgieter of the Plaintiff makes the following recommendations:

"Given the satisfactory conduct of the group together with the acceptable trading results in February 2005 reflecting on going profitability with retained earnings of R1,5 million would fully recommend continuation of facilities as currently extended including request for MTL finance of R1,079K and R570K RHL in the name of Spannenberg against variation agreement over the equity available in the RHL as security for the requested MTL.

In view of the run debt would further recommend key man insurance together with contingent liability cover be made a condition of facilities extended?

In the same document later on the same page the credit manager Nel of the Plaintiff in paragraph 3 comments ... *"The MTL will be at 44% tangibly secured given the fact that the company will be increasing Spannenberg's package to include the repayment, affordability is not the question. Spannenberg's bond will be taken over from ABSA, the variation agreement must be drawn up to secure the available equity in support of the MTL".*

⁵ Page 23(b) record.

[12] To give effect to the intention of the parties, which was to enable the First Defendant acquire the shares in the company, the following transactions took place:

12.1 The First Defendant after being contacted by one of the Plaintiff's representatives on 17 September 2005 signed an "Application for Home Loan".

12.2 On 17 October 2005 the First Defendant met with Potgieter in Mentrup's office at the premises of Airoad Express and signed a medium term loan agreement in his name for R1 079 000,00 in order to buy shares in Airoad Express ("the first medium term loan"). He also signed as director of Airoad Express (although he was as yet at that stage neither a shareholder nor director of the company) a notification of cession of the loan funds.

12.3 At the same meeting he also signed a Deed of Suretyship in terms whereof he bound himself as surety and co-principal debtor to Plaintiff for the repayment by Airoad Express of all monies owed by Airoad Express.

12.4 According to a debit order authority given to the Plaintiff by Airoad Express and on the written instructions of Mentrup, the monthly repayments in respect of the first medium term loan agreement for

R1 079 000,00 would be deducted from the bank account of Airoad Express held at the Plaintiff bank.

12.5 Thereafter, on 18 October 2005 a day after the signing of the medium term loan, Airoad Express and Mentrup sold to the First Defendant 25,1% of the shares in Airoad Express for a purchase price of R1 079 000,00⁶. On 30 November 2005 the First Defendant's gross monthly salary was increased from the previous monthly gross of R10 583,00 to R55 000,00.

12.6 From the salary advice of the First Defendant the monthly instalment due to the Plaintiff in respect of the medium term loan was deducted from the R55 000.00 monthly salary. The first such deduction, from his November salary, was R24 338,55⁷ and the monthly instalment was then debited from Airoad Express's account on or about 7 December 2005. This continued until February 2007 and during this time all monthly instalments continued to be debited from the bank account of Airoad Express.

12.7 The First Defendant on 5 December 2005 signed a Housing Loan Agreement with the Plaintiff ("the bond agreement") with account number 863121000101. In terms of this agreement a mortgage bond in the amount of R576 000,00 would be registered over the

⁶ Trial Bundle page 81(b).

⁷ Trial Bundle page 7.

Defendants' immovable property known as Erf 6270 Parow situated at 33 Jansen Street, Parow. From this amount it was agreed that R457 115,71 was to be retained, as security for the first medium term loan (R1 079 000,00), the balance was to be used to settle the Defendants' previous bond with Absa on the property mentioned above and for the payment of conveyancer's fees. According to Potgieter the monthly repayment amount was calculated on the basis of the monies drawn from the medium term loan account and as such, until the security component was used/withdrawn, the Defendants did not pay for same on a monthly basis. These monthly repayments were debited from First Defendant's account at Standard Bank.

12.8 On 9 February 2007, the Defendant signed a further Agreement of Loan constituting a housing loan under the same account number with the Plaintiff. In terms of this further bond agreement a mortgage bond in the amount of R224 000,00 was to be registered over the Defendants' property. R217 630,45 of this amount was to remain in the account as further security for the first medium term loan.⁸

12.9 On 15 March 2007, the First Defendant, at the request of Potgieter, authorised the transfer of R679 000,00 from the bond account to the

⁸ The balance of R6 396,55 was paid in respect of conveyancing fees.

credit of the account of Airoad Express⁹. The amount was apparently transferred, to reduce the first medium term loan,¹⁰ on 5 April 2007.

12.10 On 4 April 2007, the Defendant signed a further medium term loan agreement with the Plaintiff in the amount of R158 719,89. Just as in the case of the first medium term loan the monthly instalments in respect of this loan were to be debited to the account of Airoad Express. The sum of R158 719,89 was then used on the next day 5 April 2007, to settle the balance, then outstanding, of the first medium term loan.

12.11 On 10 December 2007, a second further bond agreement in the amount of R1 340 000,00 was signed by the Defendants with the Plaintiff. It essentially consolidated the amounts in terms of the original bond agreement, the first further bond agreement, and this agreement.

12.12 This second further bond agreement was as such linked to the earlier agreements and this is evident from paragraph 4 of his agreement where it is stated that:

⁹ Trial Bundle page 123(d).

¹⁰ Trial Bundle 123(d) read together with page 266.

"It is a special condition of this Agreement that payment is made to Nedbank out of the proceeds of the loan of the client's outstanding indebtedness to Nedbank in respect of loan account number ..."

12.13 In terms of this bond agreement, a further bond in the amount of R540 000,00 was to be registered against the Defendants' property. As such the total amount of R1 340 000,00 was made up of R576 000,00 being the first bond, and R224 000,00 being the second bond, and R540 000,00 being the third bond. The monthly repayments would be R16 103,63.

12.14 On the evidence, there was a disagreement as to whether the Defendants had received the full benefit of the R540 000,00 as the additional amount raised in terms of this bond. According to Potgieter the Defendants received R370 000,00 which had been used to pay a building contractor who made some renovations to their house, plus an amount of R170 000,00, which was used to cover an overdraft or bridging finance in connection with the renovations. The First Defendant however testified that they only received approximately R350 000,00 which they utilized towards renovations to their home. The First Defendant contended that R119 372,35 had been used to on 19 June 2008 to settle the balance outstanding on the second medium term loan.

12.15 As is clear from a further report by Potgieter dated 28 May 2008,¹¹ regarding the financial position of Airoad Express, on page 4 of the document, the Plaintiff, as at such date, had a “lien” over a banking account (call account) in the name of the Airoad Express as security for the medium term loan in the name of the First Defendant.

[13] The Defendants were struggling to keep up with the payments in terms of the second bond agreement and on 23 June 2008 signed a restructured agreement. Despite this arrangement the Defendants could still not keep up with the payments and stopped making the monthly payments during or about September 2009.

Arguments

[14] Mr Warner who appeared on behalf of the Defendants, argued that the underlying medium term loan agreement which gave rise to the signing of the second further bond agreement was void as being in contravention of section 38 of the Companies Act 61 of 1973 (“the Companies Act”), which was applicable at that time, and as such the said agreement upon which the Plaintiff sought to rely was unenforceable.

[15] According to him the Plaintiff was at all material times prior to the conclusion and during the implementation of the first medium term loan

¹¹ Record page 180 – 190 at page 183.

agreement aware, that the purpose of the R1 079 000,00 first medium term loan was to enable the First Defendant to buy shares in Airoad Express. Plaintiff was also aware that in order to meet the monthly instalment due to pay off this loan, Airoad Express increased the First Defendant's monthly cost to company earnings and gross income from R10 583,00 to R55 000,00. The Plaintiff was furthermore aware that Airoad Express was to pay Plaintiff the monthly instalment of the first medium term loan. This was not deducted from the First Defendant's bank account but from that of Airoad Express. This repayment source of the monthly instalment, in respect of the first medium term loan would be, inter alia, the cashflow of Airoad Express according to the evidence of Potgieter.

[16] According to Mr Warner, Mr Potgieter conceded in argument that Plaintiff would not have advanced the loans had it not been for Airoad Express's involvement. Mr Warner argued further that it was apparent from the evidence of Potgieter that no less than four bank officials (including himself) had insight into, or were involved in, the application for facilities by Airoad Express.

[17] He further argued that Potgieter conceded in cross-examination that the taking out of the second medium term loan would not have benefitted the Defendants and the only party who would have benefitted thereby would have been Airoad Express whose monthly instalments would have, as a result, decreased.

[18] He further argued that if regard is to be had to the manner in which the financing of the purchase of the shares in Airoad Express was effected, such scheme did not (for want of compliance with the various requirement thereof) fall within the ambit of Section 38(1) of the Companies Act. For this argument he placed reliance on the decision of *Lipschitz NO v UDC Bank Ltd 1979 (1) SA 789 (AD)* that an agreement in contravention of Section 38 is void and unenforceable and further submitted that it is clear from the evidence that the invitation to the First Defendant to become a shareholder in Airoad Express was only expedient in order to increase the company's BEE compliance and nothing more than that.

[19] He further submitted that since the First Defendant was not able to afford to pay for the purchase price of the shares, Airoad Express then directly and or indirectly rendered (or caused to be rendered) the necessary financial assistance to Spannenberg. This was done, so he argued, by:

- a) Arranging the medium term loan (and subsequent loans) with the Plaintiff and, in order to meet the commitments to the Plaintiff;
- b) Inflating Spannenberg 'salary' by approximately 500%;
- c) 'Deducting' the monthly instalments due to Plaintiff (in terms of the first medium term loan) from Spannenberg's inflated salary;
- d) Providing security to the Plaintiff for the loan advanced to Mr Spannenberg; and

e) Paying him a marginally increased net income.

[20] Thus he concludes that the conduct of Airoad Express was in contravention of section 38 of the Companies Act.

[21] Mr Warner submitted that the Plaintiff was, as illustrated by the evidence, through its employees in the course and scope of their employment, aware of the purpose for which the loan was given and was only willing to advance the loan to the First Defendant because of the involvement of Airoad Express and also obtained security from Airoad Express.

[22] The Plaintiff was or should reasonably have been aware that the granting of the loan in such circumstances was in contravention of section 38(1) of the Companies Act. The initial and subsequent related medium term loan was void and unenforceable.

[23] Mr Warner further submitted that the so-called "housing loans" and related mortgage bonds (all of which were under the same account number) were all, to varying degrees, granted and registered for the purpose of providing security for the void medium term loans, and are as such also unenforceable.

[24] Finally, Mr Warner argued that although the Plaintiff has handed up a Certificate providing *prima facie* proof of the Defendants' indebtedness, it has

failed to lead related evidence as to how such sum is calculated. According to Mr Warner if the court should find that the various loan agreements are void and unenforceable. He then further states that Plaintiff failed to prove what amounts, if any, is due and payable by the Defendant pursuant to the re-allocation of payments made to the amounts by which the Defendants admit that they benefitted.

[25] Mr Bremridge on behalf of the Plaintiff submits that the Defendants case is not only factually incorrect but it is also bad in law in a number of respects.

[26] Even if the Plaintiff did contravene the section, the Defendants did not seek to have the original agreement for the acquisition of shares set aside (and have not joined the seller of the shares in those proceedings), so that the relief sought by the Defendants would result in the untenable position that the agreement for the First Defendant's acquisition of the shares would stand and he would retain the shares (which would be shown to be valuable), but would be excused from repaying the funds he utilized to acquire them.

[27] In developing this argument, he submitted that the law would not countenance a position where the agreement which the Defendant alleges to contravene section 38 of the Act would stand but subsequent agreements with third parties, certain of which concluded years later, should be held void

because they are alleged to be somehow related to the allegedly infringing but unchallenged agreement.

[28] He further submitted that the Defendants' case fails to distinguish between the transaction which is alleged to provide for amount to the provision of financial assistance in contravention of section 38, and the separate agreements which contain no obligation or term for the provision of financial assistance by the company.

[29] Mr Bremridge further argued that it disregards the principles of severability as applied by the courts in relation to transactions which are alleged to contravene section 38, by failing to properly distinguish between the home loan agreement and the mortgage bonds registered to secure them.

[30] To this end he emphasized that the Plaintiff's claim is for the repayment of the funds advanced under the home loan agreement while the mortgage bonds serve only to secure such liabilities. The prohibition under section 38(1) cannot be used as a remedy or escape clause available to purchasers of shares in companies to enable them to avoid their agreements for the acquisition of shares and all related agreements. This would be a fundamental misconception and misapplication of the provision of section 38.

[31] He relied on the decision of *Lewis v Oneanate (Pty) Ltd and Another 1992 (4) SA 811 (A)*, where it was held (at 818B) that:

"The object of a provision such as s 38(1) is the protection of creditors of a company, who have a right to look to its paid-up capital as the fund out of which its debts are to be discharged. (see Trevor v Whitworth (1887) 12 AC 409 (HL) at 414.) The purpose of the legislature was to avoid that fund being employed or depleted or exposed to possible risk in consequence of transactions concluded for the purpose of or in connection with the purchase of its shares."

[32] It was submitted that the home loan and mortgage agreements which the Defendant seeks to declare unenforceable, if measured against the purpose of section 38, clearly do not offend against the provision of section 38 because they do not constitute agreements which were concluded for the purchase of shares in the company in question, Airoad Express. The said agreements also do not contain any provision for the company to give financial assistance for the purpose of the acquisition of its shares or otherwise.

[33] Mr Bremridge further argued that the Defendant bore the onus to prove that the agreements it wishes to declare void and unenforceable contravene section 38 of the Act (narrow approach).

[34] The Plaintiff argued that there was no substance to the Defendants' position that because the first medium term loan for the amount of the purchase of the shares acquired by the First Defendant, was void. Therefore

all the subsequent loan agreements (whether home loan or term loan) concluded with Plaintiff are also void. Plaintiff argued that the term loan agreement does not create any legal obligation on the company Airoad Express to make repayment of the amount of the loan advanced to the First Defendant.

[35] Furthermore, it was argued that there can be no suggestion that the agreement is in contravention of section 38, unless the court is satisfied that the salary payment and the set-off of the instalment against such salary is fictitious and that the Plaintiff was aware that this was a fictitious salary paid to the First Defendant and a party thereto.

[36] Such a conclusion so Mr Bremridge argued is totally against the evidence which showed that the salary paid to the First Defendant was properly accounted for in the books of the company and that statutory deductions for PAYE and UIF were made and are accounted for in respect thereof, as well as other deductions for medical aid and a staff loan. Furthermore, as the liability under the term loan was reduced, the First Defendant's net salary increased over time from under R10 000,00 to over R27 000,00. The reasons for this increase were due to him becoming a shareholder and director as well as his worth to the business as a BEE shareholder. The Plaintiff was therefore entitled to accept that the salary increase was commensurate with the First Defendant's increased status and position.

[37] Mr Bremridge emphasized in argument that the first medium term loan did not impose any legal obligation on the company to attend to the repayment of the loan and the deduction from the company's account was in essence a matter of administrative convenience. This fact cannot be construed to deny the reality that the obligation to repay the loan lay solely on the First Defendant. The payment was later accounted against the First Defendant's salary.

[38] It was argued that the mere fact that the First Defendant's salary was increased upon him becoming a shareholder and director is not unusual and the fact that such increase was used to acquire shares does not constitute a contravention of section 38 unless it was shown to be fictitious.

[39] It was submitted on behalf of the Plaintiff that the Defendants' reliance on the case of *Saambou Nasionale Bouvereniging v Ligatex (Pty) Ltd 1976 (1) 868 (E)* is misplaced. This case was concerned with a situation where the company in which the shares were acquired raised a loan in its own name and secured a bond over the company's property in circumstances where the lender knew that the company intended to use the loan for the purposes prohibited by section 38. The company in that instance was the borrower under the loan agreement and granted a bond over its own assets. The facts in this case are entirely different.

[40] Mr Bremridge contended that even if a transaction is deliberately constructed to avoid the prohibition in terms of section 38, it does not per se mean that it contravenes the provisions thereof. For this proposition he relied on the dictum of *Peters and Others NNO v Schoeman and Others 2001 (1) SA 872 (SCA)* at 880.

[41] In the light of the above, Mr Bremridge argued the Defendants have not satisfied the onus of showing that the first medium term loan agreement contravened section 38 of the Act.

[42] Mr Bremridge continued that the further agreements are therefore also not susceptible to challenge under section 38 of the Act. The defence therefore under section 38 must fail in its entirety.

[43] In the alternative, Mr Bremridge argued that even if the court were to be satisfied that the first medium term loan did constitute a transaction which contravened section 38 of the Act, this cannot extend to the home loan agreements concluded and certainly not to the restructure agreement concluded in 2008, being entirely separate and severable agreements. The purchase price according to Mr Bremridge was paid solely out of the proceeds of the first medium term loan.

[44] It was submitted that in order to find that any of the home loan agreements contravened section 38, the court would have to find that these

agreements imposed some obligations on the company Airoad Express or had the effect that Airoad Express thereby rendered financial assistance for the purpose of the purchase of the shares.

[45] Under these home loan agreements Airoad Express bore no obligation to the Plaintiff and it was not a party thereto. According to Mr Bremridge the evidence showed that the Defendants bore the sole obligation to repay the amounts advanced under the home loan agreements and in particular the Restructure Agreement. All the instalments were to be collected against the Defendants personal Standard Bank account.

[46] In these agreements the Second Defendant (Mrs Spannenberg) was also a party to the home loan agreement as borrower and mortgagor, though she was not a party to the term loan agreements.

[47] It was argued that for the purpose of section 38 neither the home loan agreements nor the Restructure Agreements or the mortgage bonds that secure the obligations thereunder contain any element to the effect that Airoad Express provided financial assistance for the purpose of the requisition of its shares.

[48] Mr Bremridge stated that it may well be that the First Defendant took money from his loan account to pay off a portion of the term loan obligation to the Plaintiff. That fact however does not have the effect that the home

loan agreement had been converted or transformed into an agreement whereby Airoad Express provides financial assistance for the acquisition of its shares.

[49] The Defendants' case, according to Mr Bremridge, is based on a legally unsound premise that if the agreements are somehow related to a prohibited transaction, this enables the court to strike down all the agreements. This argument is not in line with the legal position, that only if the court were to find that the agreements were indivisible or inseparable, than under such circumstances it will be struck down.

[50] According to Mr Bremridge after having referred to the decision of *Lipschitz NO v UDC Bank Ltd (supra)* and *Vernon and Others v Schoeman and Another 1978 (2) SA 305(D)* that the court do not apply section 38 on the basis of one element of a transaction may offend the provision, the entire transaction is to be declared invalid.

[51] He thus accordingly argued that even if the first medium term loan were held to contravene section 38 of the Act, it does not mean that the subsequent home loan agreements and mortgage bonds must be held to be agreements in contravention of the provisions of section 38 for the provision of assistance by Airoad Express for the acquisition of its shares.

[52] Relevant Statutory Provision – Section 38 of the Company Act 71 of 1973¹² reads as follows:

"(1) No company shall give, whether directly or indirectly, and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of or in connection with a purchase or subscription made or to be made by any person of or for any shares of the company, or where the company is a subsidiary company, of its holding company.

2) The provisions of subsection (1) shall not be construed as prohibiting—

- a) the lending of money in the ordinary course of its business by a company whose main business is the lending of money; or*
- b) the provision by a company, in accordance with any scheme for the time being in force, of money for the subscription for or purchase of shares of the company or its holding company by trustees to be held by or for the benefit of employees of the company, including any director holding a salaried employment or office in the company; or*
- (c) the making by a company of loans to persons, other than directors, bona fide in the employment of the company with a view to enabling those persons to purchase or subscribe for shares of the company or its holding company to be held by themselves as owners; or*
- (d) the provision of financial assistance for the acquisition of shares in a company by the company or its subsidiary in accordance with the provisions of section 85 for the acquisition of such shares."*

¹² A similar provision is contained in Sections 44(3) and 44(4), subject to the sections 44(1) and 44(2) of the New Companies Act 71 of 2008

[53] Issues for Consideration

The first issue for consideration is whether Airoad's actions in facilitating the initial loan agreement between the first defendant and the Plaintiff, and its inflation of the former's salary, amounted to the provision of financial assistance given by the company Airoad Express to the First Defendant for the purpose of or in connection with the purchase for the 25,1 % shareholding in the company, in contravention of section 38 of the Companies Act.

If the answer to this question is yes, the further question arises whether the first medium term loan as between the Plaintiff and the First Defendant was consequently invalid and unenforceable. The further questions are whether the subsequent home loan and mortgage loan agreements entered into between the Plaintiff and Defendant, and in particular, the second further bond agreement and subsequent restructure agreement, are also invalid and unenforceable for want of compliance with the provisions of section 38 of the Companies Act. A related issue is the severability of the subsequent loan and mortgage agreements.

[54] Analysis

The question is whether the conduct of this company amounts to financial assistance for the purposes as set out in section 38. In *Lipschitz NO v UDC Bank Ltd* (supra) at 797D, it was held that ...*"The prohibition against the giving of financial assistance is couched in very wide terms. It relates to*

"any" financial assistance, whether given "directly or indirectly" and it relates, moreover, to such assistance not only when it is given for the purpose of the purchase of or subscription for any shares in the company, but also if it is given in connection with such purchase or subscription."

[55] It is clear from the evidence that First Defendant, when he was approached by Mentrup of Airoad Express to acquire the shares was a branch manager of the company earning R10 583,00 per month. He had to purchase the shares at a cost of R1 079 000,00. He was unable to raise this money and was introduced to the bankers of the company, Nedbank ("Plaintiff"), to provide a medium term loan for this purpose.

[56] The Plaintiff was at all times aware of the purported purpose of the loan as previously pointed out, (see para 9 supra) as is clear from the document titled "APPLICATION FOR FACILITIES" relating to the financial position of Airoad Express, where the employees of the bank stated: *"We have been requested to provide medium term loan finance of R1 079K in the name of K. Spannenberg to enable the purchase of 25,1% shareholding in Airoad Express (Pty) Ltd."*

[57] For the purpose of acquiring the shares, the First Defendant was promoted to a Director and his salary was increased by 500% to R55 000,00 per month. It needs also to be mentioned that he was also appointed to this position because of his worth to the company as a BEE shareholder.

[58] The company gave the Plaintiff a debit order authority to deduct the monthly repayments of the loan from the bank account it held at the Plaintiff's bank. This amounted to approximately R24 338,55 per month which was later deducted from the salary of First Defendant.

[59] The Plaintiff stated in the document "APPLICATION FOR FACILITIES" under subheading "Security for medium term loan facility" at page 10¹³, "*The requested medium term loan to be repaid over a five year period. Spannenberg's costs to company earnings will be increased to meet this monthly instalment (additional R22K per month). He will register a bond of R720K over Spannenberg's property but will only place reliance on this security at 80% of the valuation.*"

[60] On page 11¹⁴ of the same document under subheading Credit Manager's Comments, at paragraph 3 he says: "*The MTL will be at least 44% tangibly secured, given the fact that the company will be increasing Spannenberg's package to include the repayments, affordability is not in question. Spannenberg's bond will be taken over from Absa – the variation agreement must be drawn up to secure the available equity in support of the medium term loan.*" During evidence, Potgieter of the Plaintiff conceded that the Plaintiff would not have advanced the loans had it not been for Airoad Express's involvement.

¹³ Page 23(a) Trial Bundle.

¹⁴ Page 23(b) Trial Bundle.

[61] For section 38 to be contravened two elements have to be present. The first element is that there has to be financial assistance. This includes the giving of a loan, a guarantee and the provision of security. The second element is the purpose for which the financial assistance is given. According to *R Cassim and MF Cassim 2007 SALJ 37–47* at page 41, in the article, "*Gardner v Margo: A misapplication of section 38 of the Companies Act*", if the first element of section 38 is satisfied, in that financial assistance has been given by the company, then in order to determine whether section 38 has been contravened it must still be determined whether the financial assistance was given "*for the purpose of or in connection with a purchase or subscription ... of or for any shares of the company within the meaning of the section.*"

[62] The authors goes on to say the following, "*The courts have drawn a distinction between the 'ultimate goal' of a transaction and its 'direct object', and have laid down that it is the direct object that is relevant in determining whether section 38 had been contravened, as opposed to the ultimate goal.*"

[63] In my view, the evidence shows overwhelmingly that the company by appointing the First Defendant as Director and by increasing his salary, thereby enabling him to purchase the shares, which he was previously unable to do, gave him financial assistance to do so. The salary increase to purchase the shares came directly from the company. In my view, the "direct object" was the provision of financial assistance to purchase the shares.

[64] The financial assistance did not come from an independent source. The First Defendant's salary had to be increased in order for him to have been granted the first medium term loan of R1 079 000,00 to purchase the shares in the company. This increase was effected by the company. The funding therefore to pay off the loan to purchase the shares came from the company. The company played a pivotal role in assisting First Defendant to acquire the loan and it made sure that the loan was paid off by inflating his salary. By doing this, it financed the monthly repayments of the medium term loan.

[65] According to the Plaintiff at that stage the medium term loan would be "at least 44% tangibly secured" given the fact that the company would be increasing First Defendant's package to include repayments, and that "affordability was not in question". This is a clear indication that the company increased First Defendant's salary to enable him to pay off the loan which was granted to him by the Plaintiff to buy the shares in the company. This in my view clearly falls within the conduct prohibited by section 38.

[66] *Henochsberg on the 1973 Companies Act* at 74 – 75¹⁵, commenting on section 38, states that:

"Subsection (1).—*The prohibition applies to every company having a share capital, whether it is a public company or a private company, and irrespective of the proportion of the capital constituted by the share or shares involved (Karoo Auctions (Pty) Ltd v Hersman 1951 (2) SA 33 (E) at 37). It applies whether the*

¹⁵ Also see Henochsberg's comment on Section 44 of the Companies Act 71 of 2008 Vol 1at 185-186.

financial assistance is, or would be, given to the purchaser or the subscriber or to another, provided it is, or would be, given for the purpose of, or in connection with, the purchase or subscription (Jacobson v Liquidator M Bulkin & Co Ltd 1976 (3) SA 781 (T) at 787–788; Armour Hick Northern Ltd v Armour Trust Ltd [1980] 3 All ER 833 (Ch) at 837)."

"The prohibition . . . comprises two main elements; one is the giving of financial assistance, the other is the purpose for which it is given (or the 'in [Page 75] connection with' provision). The two elements are linked to form a single prohibition, but although so linked they are vitally different in concept" (per Miller JA in Lipschitz NO v UDC Bank Ltd 1979 (1) SA 789 (A) at 799). It is respectfully submitted that the fundamental enquiry in each case involving a sale of shares is whether the effect of the particular transaction is that the company has given, or would give, financial assistance and, if so, was it, or would it be, given for the purpose of, or in connection with, the purchase of the shares (Gradwell (Pty) Ltd v Rostra Printers Ltd 1959 (4) SA 419 (A) at 424–426 as explained in the Lipschitz case supra at 798–801; and see at 803–805; Miller v Muller 1965 (4) SA 458 (C) at 465–466; Zentland Holdings (Pty) Ltd v Saambou Nasionale Bouvereniging 1979 (4) SA 574 (C) at 577–578). "In Gardner v Margo [2006] 3 All SA 229 (SCA), the Court approved the distinction drawn in the Gradwell case between the "ultimate goal" of the transaction and the "direct object" of the transaction, and that it is only the "direct object" which is relevant thus (at 243): "If the direct object is not the provision of financial assistance by the company for the purpose of or in connection with a purchase of its shares, then it is irrelevant if the ultimate goal of the transaction is to enable the person to purchase such shares." See R Cassim and MF Cassim 2007 SALJ 37–47 for a discussion of the Gardner case supra."

Henocheberg further states at page 75:

"If the purpose of the company in giving the financial assistance was not, or would not be, in fact the purpose of the purchase of its shares (ie the prohibited purpose), it cannot be held that the giving of such assistance was, or would be, "in connection with" the purchase of the company's shares, within the meaning of the subsection, unless the actual purpose sufficiently closely resembles the

prohibited purpose (ibid at 804–805). For an example of a case where it was held that the purpose of the transaction was too remote from the prohibited purpose, see Pires v American Fruit Market (Pty) Ltd 1952 (2) SA 337 (T). The prohibition in s 38 (1) is "not contravened when the direct object of the transaction is merely to give another that to which he or she is already entitled" (Gardner case supra at 243 d–e), since in those circumstances the direct object of the transaction is not the giving of financial assistance."

[67] In my view, therefore, the medium term loan granted to the First Defendant by the Plaintiff in order for the former to acquire the shares in the company was advanced by the Plaintiff to the First Defendant, with the knowledge of the Plaintiff which is financial assistance by the company in contravention of section 38.

[68] The next question that arises, is whether the subsequent home loan agreements were entirely separate and severable agreements, whose validity for the purposes of section 38 of the old Companies Act must be judged on their own terms. The Plaintiff reminded the Court that to find that any of the home loan agreements contravened section 38, it had to find that they imposed obligations on the company Airoad Express or had the effect that Airoad thereby rendered financial assistance for the purpose of the purchase of its shares. The Plaintiff, however, argued that the company in the circumstance bore no obligation to the Plaintiff as lender, in respect of the home loan agreements, and was in fact not a party thereto.

[69] Counsel for the Plaintiff argued indeed, that such agreements are indeed entirely separate and severable, drawing attention to the facts that, firstly, the defendants bore the sole obligation to repay the amounts advanced under the home loan agreements and the Restructure Agreement and all instalments were to be collected against the defendant's personal account, and secondly, the agreements were concluded with the second defendant as borrower and mortgagor.

Counsel relied on the judgment of *Vernon & Others v Schoeman & Another (supra)* where *Hefer J* (as he then was) held at 307H:

"It is trite that, where an agreement contains an unenforceable provision, the whole agreement is not necessarily void and that the enforceability of its other provisions depends on whether they are severable from the unenforceable one."

[70] The Plaintiff's contentions in my view are not consistent with the true facts of this case and the facts in this case are distinguishable from that in the *Vernon v Schoeman* case (*supra*). While it is true that these agreements were solely between the Plaintiff and Defendants, it was inextricably linked to the medium term loan agreement which the Plaintiff advanced to the First Defendant to acquire the shares in the company. In *Lipschitz NO v UDC Bank Ltd (supra)* at 807G – 808A – D it was held:

"The primary question whenever a Court is asked to uphold the good while rejecting the bad part of a contract is whether the contract is divisible in that

respect. (In Spink's case supra at 601 the relevant portions of the agreement were held to be "perfectly severable".) Here we are concerned with a provision as to guarantee which was undoubtedly inserted for the benefit of the lender, UDC. Clearly, UDC could elect not to prefer any claim on the cross-guarantee. But that circumstance alone does not render the agreement divisible. It is true that the cross-guarantee was in form a separately executed contract of suretyship between UDC and the signatories thereto but, in the circumstances of this case, it would be unrealistic in the extreme to regard it as independent of, or as anything other than an agreement fully integrated with, the loan agreement. It is very clear that UDC was prepared to lend to Ubco the sum of R87 000 only if certain conditions, including the provision of the cross-guarantee, were met. UDC required not only each of the companies to bind itself as guarantor, but it also required Baker, who controlled all three companies, so to bind himself. The aim, clearly, was to obtain the greatest possible degree of cover for this, the second loan, and at the same time to increase the cover in respect of the money already advanced in terms of the first loan. The separate document recording the cross-guarantee was undoubtedly an essential and integral part of a design for the obtaining of the second loan and it was no less an integral and inseverable part of such design and of the loan agreement than it would have been had all been contained in one document signed by all the parties concerned and clearly reflecting the provision of the cross-guarantee as a condition of the granting of the loan. The agreement of loan, therefore, was in breach of s 86 bis (2) and illegal and I am unable to accept (with due respect to certain observations made by CROSS J in the South Western Mineral Water case supra at 958B - E) that it could thereafter be rendered lawful by a decision by UDC not to found a claim on the cross-guarantee or by any other unilateral act by UDC or any one of the parties to the agreement." (own emphasis)

[71] Right from the onset, the Plaintiff insisted that a bond be registered over the property as security for the medium term loan of R1 079 000,00 advanced to procure the shares in the company. In its "APPLICATION FOR

FACILITIES” at page 10¹⁶ under the heading “SECURITY FOR MTL FACILITY” the Plaintiff indicates that it will register a bond of R720K (value of First Defendant’s property) but will only place reliance on this security at 80% of the valuation which is R576 000,00. At that stage there was clearly no need for the Defendants, who had an outstanding bond of R108 000,00 with Absa, to register a bond with the Plaintiff over their property in the amount of R576 000,00 other than to secure the medium term loan. Thereafter a second bond, once again, of R224 000,00 was registered over the Defendants’ property of which R217 630,45 was to remain in the account as further security for the first medium term loan.

[72] On 15 March 2007, an amount of R679 000,00 was transferred from the bond account to credit the account of Airoad Express. On 4 April 2007 the First Defendant signed a further medium term loan agreement in the amount of R158 719,89. The monthly repayments in respect of this loan were to be debited to the bank account of Airoad Express. This sum of R158 719,89 was then used to settle on 5 April 2007 the balance outstanding of the first medium term loan.

[73] On 10 December 2007, the Defendant signed a further agreement of loan under the same account of R1 340 000,00, the amount now claimed in terms of the Particulars of Claim.

¹⁶ Trial Bundle 23(a).

[74] The total amount was made up of R576 000,00 (the first bond to secure the medium term loan) plus R224 000,00 being the second bond to secure and pay off the medium term loan advanced to acquire the shares and an amount of R540 000,00. The home loans in respect of the amounts of R576 000,00 and R224 000,00 were used as security for the medium term loan which was used to acquire the shares. These loans were advanced for no other reason than to secure the medium term loan and cannot be regarded as separate from it.

[75] Just as in the *Lipschitz* case the Plaintiff in this case insisted that a separate agreement be concluded in terms of which a bond and a home loan were advanced to secure the loan in terms of which the shares were purchased. The Plaintiff clearly would not have granted the medium term loan had this condition not have been met.

[76] The Plaintiff was a third party to the agreement between the company and the First Defendant and was aware of the assistance given to the First Defendant. *Henochsberg* at 77 as supported by *AJ Kerr 1976 SALJ 3*; *R C Beuthen 1976 Annual Survey 306 – 307* and *AN Oelofse in General Note 55-57*, contrary to the decision of *Manufacturers Development Co (Pty) Ltd v Diesel and Auto Engineering Co 1975 (2) SA 776 (W)*, where the author states:

*"But an agreement between the company and a third party – ie someone other than the seller or the purchaser of the shares – by which eg the company obtains money which it intends to use in contravention of s 38(1) is not void where the third party is unaware of such intention (Saambou Nasionale Bouvereniging v Ligatex (Pty) Ltd 1976 (1) SA 868 (E)). Notwithstanding Manufacturers Development Co (Pty) Ltd v Diesel & Auto Engineering Co 1975 (2) SA 776 (W), it is respectfully submitted that if the third party knows that the performance in terms of his agreement with the company is to be used by the latter to contravene s 38(1), such agreement is void (cf AJ Kerr 1976 SALJ 3; RC Beuthin 1976 Annual Survey 306–307; AN Oelofse op cit in the **General Note** 55–56). It is also void, it is respectfully submitted, if it is an inseparable part of an agreement by which the company gives, or is to give, financial assistance, within the meaning of s 38(1) (Lipschitz case supra at 807–808)."*

I agree with this contention and I am of the view that the same reasoning can be applied in this case in relation to a situation where a third party (bank) knowingly (prospective shareholder) aided and facilitated the company to financially assist another in acquiring shares in that company.

[77] This is clear from the evidence of Potgieter. And also what was contained in the Plaintiff's document entitled "APPLICATION FOR FACILITIES" about how it set out to assist and aid Airoad Express in facilitating the First Defendant to acquire the medium term loan to buy the shares in the company. It also obtained security from Airoad Express for this purpose. Plaintiff throughout was or ought reasonably have been aware that the granting of the medium term loan in such circumstances was in contravention of section 38 of the Companies Act.

[78] These two home loans can therefore not be severed from the prohibited agreement because it was used to secure the agreement in contravention of section 38 and it is inextricably linked to it. It is not a separate agreement independent from the first medium term loan agreement. In the result therefore I find that the initial and subsequent medium term loan void and unenforceable. I also find that the housing loans and mortgage bonds in the amount of R576 000,00 and R224 000,00 granted and registered for the purpose of providing security for the void medium term loan are also unenforceable.

[79] This brings me to the next question, which is the amount that the Defendants are indebted to the Plaintiff where it was not used for the purposes of acquiring the shares.

[80] There was disagreement on the evidence as to whether or not Defendants had received the benefit of the full amount of R540 000,00.

[81] Mr Potgieter testified that Defendants had received the full benefit of the R540 000,00; R370 000,00 having been used to pay the building contractor and R170 000,00 to cover an overdraft or bridging finance used before hand in connection with the renovations. First Defendant testified that they had received the benefit of approximately R350 000,00 that was used towards the renovations and that, ultimately, R119 372,85 had been used, on

19 June 2008, to settle the balance outstanding on the second medium term loan.

[82] It is difficult to find on the evidence whether the Defendants are indebted to the full amount of R540 000,00, as submitted by Plaintiff, to make up the final amount of R1 340 000,00, or to the amount of R350 000,00 which the Defendants admit that they are indebted to the Plaintiff. From the evidence it is common cause that the amounts of R576 000,00 plus R225 000,00 were used from the home loans to pay off the medium term loan.

[83] The Defendants also admitted that they have received the further benefit of R108 109,33 that was paid to settle their bond with Absa. These amounts according to the evidence constitute the only lawful benefit the Defendants have received in terms of the loans advanced by the Plaintiff and which they are liable to pay.

[84] Although the Defendants conceded that they are indebted to the Plaintiff in the amounts of R350 000,00 and R108 109,33, it would be unfair to dismiss the Plaintiff's case in its entirety where a concession was made that they are at least indebted in the amount as mentioned. Mr Bremridge argued that as a result of this dispute, as to how exactly the R540 000,00 was utilized further evidence should be led to quantify the amount owing if the Court

should find that there is a reduction in the amount due to the provisions of section 38.

[85] Mr Warner on behalf of the Defendants argued that absolution from the instance be granted against the Plaintiff in respect of any claims that may have arisen pursuant to the Defendants' admission that they had benefitted from certain income advanced by the Plaintiff.

[86] Whilst I understand the dilemma Mr Bremridge found himself in, I am not sure whether it is legally permissible for this court at the end of the proceedings, during the judgment stage, to make such an order. I am however more inclined to follow the route suggested by Mr Warner and I have found authority for this proposition.

In Herbstein and Van Winsen Vol 1 (5ed) at 924 it is stated ... "Although there is no express provision in rule 39 for an order for absolution from the instance at the conclusion of the whole case, the practice to grant absolution when a Plaintiff has not established the facts in support of his case to the satisfaction of the court, has been extended to cases in which evidence for the Defendant had also been given."

In Zeffert and Paizes (formerly Hoffman and Zeffert), the Law of Evidence (2nd ed) at 178 the authors hold the view that ... "It is the appropriate order when after all the evidence the Plaintiff has not discharged the ordinary

burden of proof. Its procedural advantage is that it enables the Plaintiff to bring another action on the same facts; a privilege which is denied to the Defendant of the facts in an action in which the burden is upon him."

And further at 933 the learned author states:

"In civil cases it should be noticed that the practice of granting absolution from the instance tends to mean that finality is sauce for the defendant but not for the plaintiff. A plaintiff who fails to prove his case may claim that the court should order absolution rather than judgment in favour of the defendant and this gives him a right to a new trial. So, in Deintje v Grains and Gratus, the Appellate Division refused leave to adduce further evidence but altered the order of the court below from judgment for the defendant to absolution. In such a case the court's choice is not between re-opening the case and finality, but between re-opening one issue and re-opening them all. Logically, therefore, the only consideration in making the choice should be whether the opposing party might be prejudiced by not having the other issues retried, but so far the courts have not attempted to relate the rules for permitting further evidence to the practice of granting absolution."

[87] I am therefore in agreement with Mr Warner when he called for the court to make such an order.

[88] Order

In the result I make the following order:

- 1) That the Plaintiff's claim based upon, or arising from, the medium term loan for R1 079 000,00 (including the subsequent medium term loan and all "bond" loan agreements) is dismissed;
- 2) That absolution from the instance be granted against the Plaintiff in respect of any claims that may have arisen pursuant to the Defendants' admission that they had benefitted from certain monies advanced by the Plaintiff;
- 3) That mortgage bonds No.'s B138021/2005 (in the amount of R576 000,00) and B22367/2007 (in the amount of R224 000,00) registered over the Defendants' immovable property known as Erf 6270, Parow and situate at 33 Jansen Street, Parow, are invalid and unenforceable; and
- 4) Mortgage bond B18842/08 also registered over the Defendants' immovable property as mentioned (in the amount of R540 000,00), is also invalid and unenforceable only insofar as it relates to the indebtedness which the Defendants have not admitted to.
- 5) Plaintiff pays the Defendants' costs.

HENNEY, J

Judge of the High Court

