<u>DISTRIBUTABLE</u> (34)

(1) ELIAS HWENGA (2) MERCY HWENGA (3) KENNETH (4) PRINCE NYEMBA (5) A. P. PHILLIP AND COMPANY (PRIVATE) LIMITED
v
FBC BANK LIMITED

SUPREME COURT OF ZIMBABWE
GWAUNZA JA PATEL JA & MAVANGIRA JA
HARARE MARCH 2, 2017

T. Magwaliba, for the appellants

T. Mpofu with *N. Chamisa* for the respondent

MAVANGIRA JA: After hearing the parties on 2 March 2017 this Court pronounced:

> "It is the unanimous view of this Court that the appeal is devoid of merit and ought to fail. Accordingly, it is ordered as follows:
> The appeal is dismissed with costs.
> Reasons for this judgment will follow in due course."

The following are the reasons.

FACTUAL BACKGROUND

The judgment of the court *a quo* sets out the full facts of this matter. I will extract therefrom the salient facts pertinent to this appeal. The respondent and United Builders Merchants (Pvt) Ltd (UBM) entered into a composite loan facility and guarantee agreement on 26 August 2013. In terms of the agreement, the respondent granted a medium term loan facility and guarantee agreement to UBM whereby it advanced the sum of $937 000.00 together with a medium term bank guarantee facility in the sum of $63 000.00 to provide UBM with working capital.

To secure the facilities, mortgage bonds were registered over properties belonging to the appellants who were all directors in UBM. The bank guarantee was to expire on 31 December 2013 with the loan facility expiring on 31 December 2016. Subsequent to the agreement, on 27 November 2013, UBM applied for and obtained an order in terms of s 191 of the Companies Act [*Chapter 24:03*] under HC 9992/13 to enter into a scheme of arrangement with its creditors.

A scheme of arrangement was approved between UBM, its members and creditors with the respondent as the secured creditor. It was agreed at the scheme of arrangement meeting that the terms of the Secured Creditor's Scheme of Arrangement were to be the terms contained in the facility letter dated 26 August 2013. The main features of the scheme of arrangement were a joint venture agreement between UBM and P and L Hardware (Pty) Ltd, a South African company, to become UBM P and L (Pvt) Ltd (the joint venture company).

UBM proceeded to draw down on the facility in the sum of $1 000 000.00 and it failed to pay back the said amount. Subsequently, the respondent applied for the setting aside of the scheme of arrangement and proceeded to institute proceedings against the appellants for the discharge of their obligations as guarantors for the payment of $1 141 260.36, jointly and severally.

THE COURT *A QUO'S* DETERMINATION

After considering the evidence placed before it, the court *a quo* found in favour of the respondent and granted its claim. The court noted that the major changes made in respect of the scheme of arrangement were the joint venture agreement and the extension of time within which the obligation was to be met. The said extension was given after the debt had become due and payable as the principal debtor was already in default.

The court *a quo* further found that the application to set aside the scheme of arrangement had no relevance to the question of the liability of the appellants. The court reasoned that the matter stood to be decided on the terms and the wording of the guarantees signed by the appellants in favour of the principal debtor (UBM). The court found that a surety or guarantor is not necessarily released from liability where the agreement between the creditor and principal debtor is novated. It stated that, as was the position in this case, where a surety or guarantee agreement contains a special clause which excludes certain arrangements, such as compromise, set off and novation, which would have otherwise released him, the surety is not released from liability.

The court *a quo* further highlighted that the terms of the guarantee agreement revealed that the parties had contracted to exclude the rights of novation and had evinced a clear intention to exclude such rights. It held that clause 1 contained an express term excluding the right to novation of a debt. It noted that clause 5 made it clear that no insolvency or compromise of the debt would prejudice the bank's right to recover to the full extent of the guarantee. The court found that taking into account the *caveat subscriptor* rule, the appellants were bound by their signatures as affixed to the agreement. Accordingly, the court *a quo* made an order in the following terms:

"In the result it is ordered as follows:
1. The defendant's claim in reconvention is dismissed.
2. The plaintiff's claim is upheld.
3. The defendants are jointly and severally, with one paying the others to be absolved to pay,
   a) The sum of $1 141 260.36
   b) Interest on the sum of $1 141 260.36 at the rate of 35% per annum calculated from 1 April 2014 to the date of payment in full.
4. Stand 309 The Grange Township of Stand 1 of the Grange Township in the District of 8 Salisbury, held under Deed of Transfer number 27261/2002 is hereby declared especially executable.
5. Stand 24 Winchedon Township of Lot D of Borrowdale Estate in the District of Salisbury, held under Deed of Transfer number 9730/2003 is declared especially executable.
6. Stand 62 Luna Township of Subdivision K of Luna of Section 4 Borrowdale Estate in the District of Salisbury, held under Deed of Transfer number 8011/98 is declared especially executable.
7. Costs of suit (sic)

THIS APPEAL

The appellants have now appealed to this Court challenging the correctness of the decision made by the court *a quo*. The appellant's contention before this Court is that the court *a quo* erred in making a finding that the respondent did not sue the appellants in terms of the Banking Facilities Agreement of 26 August 2013. They contend that the matter proceeded by way of a stated case in terms of r 199 of the High Court Rules, 1971.

In terms of the stated case, the appellants submitted that the parties were in agreement that the respondent was suing in terms of the Banking Facilities Agreement. Thus, the deeds of suretyship on their own could not have formed the basis upon which the respondent could sue the appellants. The appellants argue that the deeds of suretyship were ancillary agreements and should have been read together with the principal agreement, being the Banking Facilities Agreement.

The appellants further contend that the compromise, being a form of novation, substituted the original cause of action completely and conclusively.

The respondent on the other hand contends that what ought to be considered by this Court is the effect at law of the clear provisions of the deeds of suretyship. The respondent argues that the terms of the said deeds were to the effect that the appellants freely and voluntarily entered into a suretyship agreement which could not be altered even by novation. It contends that this appeal thus lacks merit.

ISSUE FOR DETERMINATION

The issue for determination is whether the compromise agreement resulted in a novation of the deeds of suretyship, thereby extinguishing the appellants' obligations as sureties.

THE LAW AND ITS APPLICTION TO THE FACTS

The meaning or definition of a compromise is aptly captured by the learned author RH Christie in *Business Law in Zimbabwe* (1st ed, Juta & Co Ltd, cape Town 1998) at p 108 as follows:

> "Compromise is the settlement by agreement of disputed obligations and is a form of novation, replacing the disputed obligations by the obligations created by the arrangement of compromise." (the underlining is added)

As correctly stated by the court *a quo,* the effect of a compromise is that it bars any proceedings based on the original cause, unless there is an agreement to the contrary.

For the purposes of this judgment, regard must be had to the meaning and import of both a "compromise" and a "novation". Christie also explains the concept of novation at p107 in the following terms:

> "Novation means the replacing of an existing obligation by a new one, the existing obligation being thereby discharged … Because novation involves a waiver of existing rights it follows that it will not be presumed and, as held in *Ballenden v Salisbury City Council* 1949 SR 269 at 273; 1949 (1) SA 240 at 246, it must be strictly proved."

The court *a quo* appropriately articulated the sentiments of Gibson's *Mercantile and Company Law in South Africa* and Caney's *Law of Suretyship,* on p 5 of its judgment when it stated:

> "… the authors deal with the question regarding whether an extension of time to pay granted by the creditor to the principal debtor can discharge the surety. The authors state that if the agreement between the creditor and principal debtor amounts to a novation, the surety is discharged. They rely for this proposition on the *Estate Liebenberg v Standard Bank of South Africa* 1927 AD 502 at 507. They make the observation that an extension of time granted <u>after the debt has become due</u> cannot be regarded as novation and the surety is not discharged. The authors state that where the extension is granted by agreement of the creditor and the principal debtor before the debt has become due, without the consent of the surety, the surety is usually released."

In casu, the appellants allege that the compromise agreement was a form of novation which extinguished their obligation to honour the deeds of suretyship. However, they failed to prove that when the compromise agreement was effected the debt had not yet become due. They also failed to prove that they did not consent to be held as sureties in the event that the original agreement was altered.

It is apparent, that in terms of the Bank Facilities Agreement, the amounts lent became due and payable on 31 December 2013. The scheme of arrangement was only entered into after the principal debtor had failed to meet its obligation to pay on time. It is also apparent that the appellants signed guarantees that bound them as sureties even in the event that the agreement was novated. Clause 1 of the guarantee agreement provides undertakings in the following terms:

> "I the undersigned … do hereby guarantee and bind myself as surety for the repayment on demand of all sum or sums of money which the debtor may from now or from time to time hereafter owe or be indebted in to the Bank its successors or assigns whether such indebtedness be incurred by the Debtor in ITS own name or in the name of any firm in which the Debtor may be trading either solely with others in partnership or otherwise, and whether such indebtedness arise from money already advanced or hereafter to be advanced … <u>or in respect of any indebtedness which may take the place of any novated debt, even if such novation takes place after the termination of this guarantee</u>, or otherwise …" (the underlining is mine)

The appellants clearly and unequivocally bound themselves as sureties to the original debt and even to a novation of that debt, by entering into an agreement that bound them even in the event of a novation or compromise.

In *Zimbabwe Football Association v Mafurusa* 1985 (1) ZLR 244, the court stated:

> "What is the effect of this novation on the defendant's liability as guarantor – does it mean, as he says, he is discharged from all his obligations under the deed of undertaking? I do not think so. The plaintiff agreed to lend money to the principal debtors on condition that someone guaranteed repayment. The defendant provided this guarantee. The extent of his liability as guarantor was co-extensive with the liability of the principal debtors, namely that as the whole amount was payable by him on the agreed date by the principal debtors, so the whole amount was payable by him at once in the event of the principal debtors defaulting. The principal debtors defaulted, but the plaintiff, instead of pressing for its milligram of flesh under the existing agreement, not only granted an extension of time to the principal debtors but allowed them to pay the debt in monthly instalments and without any penalty clause. But this new repayment agreement between the plaintiff and the principal debtors did not and could not discharge the defendant as guarantor. The new agreement only affected the extent, not the nature, of his obligation to the plaintiff, because the plaintiff still needed a guarantee that it would be paid. But instead of being liable for the whole amount at once in the case of default, the defendant became under the new agreement only liable to the extent of the unpaid instalment(s)."

The *Mafurusa* decision *supra* has been widely criticised as its net effect was that it is not every case of novation that will discharge a surety. However, it is settled that once an agreement is novated the surety is discharged. What transpired in that case was an extension of time to settle the amount. In that regard, such an agreement cannot be said to be a novation for the purposes of discharging a surety.

In *Estate Liebenberg v Standard Bank of South Africa* 1927 AD 502, the court held that:

> "It must be accepted that by our law not every extension of time is considered to effect a novation. If novation is given after the debt becomes due and payable, when the debtor is in *mora*, then a failure to sue the debtor or even the granting to him of an extension of time cannot be regarded as a novation therefore the surety is not discharged. He can be released if he shows that he suffered prejudice."

In *casu*, the principal debtor was granted an extension of time by the respondent. Not much changed from the original agreement save for the joint venture arrangement. Thus, the sureties could not be discharged simply on the basis of the alteration to the agreement.

As stated by the court *a quo*, the case before it stood to be decided on the terms and the wording of the guarantees signed by the appellants. In *ZIMRA v Mudzimuwaona* SC 4/18, GOWORA JA stated:

> "… the principle of sanctity of contracts confines the court only to interpreting a contract and not creating a new contract for the parties. It entails that the court should respect the contract made by the parties and give effect to it."

In Caney's *The Law of Suretyship* at p 109 the following explanation is given:

> "The intention of the parties is determined by the language used, giving effect to the ordinary meaning of their words and to the grammatical sense in which they have expressed themselves, unless if it appears from the context that both parties intended their language to bear a different meaning. If the language is clear, we must give effect to it and in so doing presume that the parties knew the meaning of the words used."

As already stated, it is apparent that the guarantees that were signed excluded rights of discharge that flow from novation. There is nothing in our law that precludes parties from entering into such an undertaking.

It is for these reasons that we found that the appeal had no merit and proceeded to grant the order that we did as recorded at the beginning of this judgment.

GWAUNZA JA I agree

PATEL JA I agree

Wintertons, appellants' legal practitioners

Mawere and Sibanda, respondent's legal practitioners