IN THE HIGH COURT OF SOUTH AFRICA

GAUTENG DIVISION, PRETORIA

20/5/16

CASE NO: A803/2014

In the matter between:

GRINDROD BANK LIMITED Appellant

and

(1) REPORTABLE: ~~YES~~ / NO

(2) OF INTEREST TO OTHER JUDGES: ~~YES~~ / NO

18/05/16
DATE

SIGNATURE

JEREMY ARTHUR TORODE NO First Respondent

CAROL-ANNE TORODE NO Second Respondent

DEE-BRONWYN BEZUIDENHOUT NO Third Respondent

JEREMY ARTHUR TORODE Fourth Respondent

JUDGMENT

Tuchten J:

1 This appeal and cross-appeal arise from a loan made by the appellant (the Bank) to the Sarnia Trust (the Trust). The first, second and third respondents were cited as its trustees. The fourth respondent (Torode) in his personal capacity stood surety for the Trust's obligations. It is common cause that the money was indeed advanced

to the Trust but the Trust and Torode resisted the Bank's claim for repayment on a number of grounds, which when the matter came to trial, reduced to the proposition that the loan agreement was invalid because the transaction contravened s 38 of the Companies Act, 61 of 1973 (the old Companies Act) and that the loan agreement between the Bank and the Trust was a simulation, unlawfully designed to evade the provisions of s 38. It was not controversial that if the Trust is not liable on the loan agreement, Torode is not liable in the present case as surety because his liability is accessory to that of the Trust. In addition, the respondents brought a claim in reconvention, reclaiming the amounts paid to the Bank under the allegedly invalid loan agreement under the *condictio indebiti* and seeking to have Torode's suretyship and the mortgage bond passed by the Trust pursuant to the loan agreement declared invalid.[1]

2 In the court below, Phatudi J found against the Bank on the main claim, on the ground that the loan agreement indeed contravened s 38 and against the Trust on the claim in reconvention on the ground that the Trust knew full well that the loan agreement contravened s 38 and was thus *in pari delicto.* Both the Bank and the Trust were in a

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[1] We were told from the bar that there is a further action pending between the same parties in which the Bank seeks to hold the Trust liable for the monies advanced on the basis of unjustified enrichment and Torode liable on the suretyship. Nothing in this judgment should be taken as an expression of opinion on the merits of that action.

measure aggrieved by the judgment in the court below. Hence the present appeal and cross-appeal.

3 The loan, of R2 million, was needed to fund the commercial activities of a company called Umoya Airtime Solutions (Pty) Ltd. Umoya was desperately in need of finance. It owed substantial amounts to its creditors, particularly to CES, the manufacturer of its product, to which it owed in 2009 between R600 000 and R 800 000. This product was a terminal which enabled vendors to sell airtime ultimately used by devices for electronic communication. Those with commercial interests in and around Umoya thought the product had great commercial potential but had been unable to raise the capital needed to exploit the opportunity effectively. An application made to Absa for finance had been rejected and there is no suggestion that any other financial institution would lend Umoya money.

4 At the time relevant to this case, Umoya's shares were held by two persons: Mr White, who held 90% and Mr Lambert, who held 10%. Torode had previously lent White, the principal shareholder in Umoya and at that time a good friend of Torode, R500 000. White repaid half of the loan soon thereafter and Torode took the balance in Umoya's product. It seems that White had accepted liability towards Umoya for product supplied to Torode, a liability which White had discharged, or

agreed to discharge by an adjustment of his loan account in Umoya. Torode had appetite to increase his investment in Umoya by the provision of what in effect was venture capital. But Torode needed to borrow the money for his anticipated investment. Through the Trust, Torode had an asset in the form of a property in Gauteng (the Gauteng property) which could be put up as security. Torode and White agreed in principle that against payment of the amount of R2 million which would be used for the benefit of Umoya, White would transfer 45% of the issued shares in Umoya to the Trust. This would make White and Torode, through the Trust, each 45% shareholders with Lambert continuing to hold the remaining 10%.

5 Torode approached Mr Olivier, an employee of the Bank, and explained the transaction to him. The Bank agreed in principle to advance the loan to the Trust. The Bank required Torode in his personal capacity to guarantee the obligations of the Trust. It also required Umoya to guarantee the obligations of the Trust to the Bank. This was because the Bank identified the Trust as the ultimate beneficiary of the funds (correctly so, from a commercial perspective) and the only potential source of income from which to repay the loan.

6 A loan agreement was drawn by the Bank. It took the form of a letter dated 3 September 2009 in which a "term loan facility" was offered to the Trust. The offer of the term loan facility was accepted by the Trust on 8 September 2009. I shall call this document the initial facility.

7 After reciting that the term loan facility was for R2 million to be lent to the Trust, defined as "the Borrower", the initial facility recorded the following under the heading "FACILITY AMOUNT":

> The facility is for an amount of R2 ... million ... which will be utilised for the acquisition of 45% shareholding in Umoya Solutions (Pty) Ltd ("the Company").

8 The initial facility proceeded to regulate, similarly under headings, such matters as interest, the term of the facility, repayments, a valuation and the insurance of the Gauteng property and several "SPECIAL CONDITIONS", which included special condition AD:

> The Bank requires the Company's Shareholders' Agreement acknowledging the Borrower's investment in the Company as well as the Bank's facility to the Borrower. The Shareholders Agreement should incorporate that the Company is responsible for the monthly repayment of capital and interest on the facility.

9 Paragraph 5, under the heading "SECURITY" included requirements that the Trust as Borrower register a first covering mortgage bond over the Gauteng property and that Torode personally sign an unlimited guarantee in favour of the Bank. It also provided in paragraph 5(d):

> The Company shall sign an unlimited guarantee in favour of the Bank.

10 It became common cause before us that the initial facility in fact contravened s 38 of the Companies Act, 61 of 1973 (the old Companies Act), which was in force at the time. Section 38 provided at the time as follows, under the heading "No financial assistance to purchase shares of company or holding company":

> (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.

(2A) Subsection (1) does not prohibit a company from giving financial assistance for the purchase of or subscription for shares of that company or its holding company if -

(a) the company's board is satisfied that -

(i) subsequent to the transaction the consolidated assets of the company fairly valued will be more than its consolidated liabilities; and

(ii) subsequent to providing the assistance, and for the duration of the transaction, the company will be able to pay its debts as they become due in the ordinary course of business; and

(iii) the terms upon which the assistance is to be given is sanctioned by a special resolution of its members.

(3)(a) Any company which contravenes the provisions of this section, and every director or officer of such company, shall be guilty of an offence.

(b) For the purpose of this subsection 'director', in relation to a company, includes any person who at the time of the alleged contravention was a director of the company.

(c) It shall be a defence in any proceedings under this section against any director or officer of a company if it is proved that the accused was not a party to the contravention.

11 The Bank received legal advice on the s 38 issue. Its attorney, Mr Green of the firm Cox Yeats, wrote the Bank a letter dated 14 September 2009 in which he advised:

> If [Umoya] is required to stand guarantee for the obligations of a shareholder then that act will need to be authorised by a Special Resolution passed by the shareholders in [Umoya] by a 75% vote and registered with the Registrar of Companies.

Section 38(1) imposed a general prohibition. Green's reference to a special resolution related manifestly to the exception to the general prohibition created by s 38(2A).

12 Olivier had a number of consultations with the Bank's legal advisors. The advice of Green was, and was understood by Olivier to be, that there was a concern that the proposed transaction would fall foul of s 38 but that this concern could be eliminated if a special resolution

were passed with the requisite majority by the shareholders of Umoya and registered.

13 On 15 September 2009, Olivier sent an email to Torode and White. Olivier began the email by stating that he had "more unpleasant news for all". He gave the text of s 38(1) and continued, in numbered paragraph 1:

> This means that Umoya cannot guarantee the loan to the ... Trust as we would be contravening the said Act, albeit the shares are being traded for a nominal par value. From our side, it is imperative that Umoya stand guarantee as they are the means to the serviceability of debt. Cox Yeats has agreed that a Special Resolution be drafted by Gavin Price Attorneys (i.e. Gavin Price Attorneys are drafting the shareholder's agreement). I am not privy to the wording of the said resolution. Cox Yeats has requested a copy of the Shareholder's agreement to ratify the 'terms' of the shareholder's loan etc.

14 In numbered paragraph 2 of the letter, Olivier referred to a further item of unpleasant news:

> I mentioned to all (Umoya and [the Trust] & Gavin Price) that we would be able to pay-out on signing and lodgment of the said Bond documents, but this request has been denied by my Management. I was under the impression that this was

> the norm, and I naively committed as much to all. My sincere apologies for the misleading information.
> It is therefore recommended that the Company [ie Umoya] approach a bridging finance company for the required amount as the payout, from our side will only occur once the following has transpired:
> - The Sarnia Trust Loan Agreement signed.
> - The Umoya Guarantee signed.
> - All FICA information is in place & the valuation is acceptable to the Bank.
> - Bond documents signed.
> - Sight of Shareholder's agreement.
> - Resolution drawn-up regarding Section 38.
> - Bond lodged and registered.

15 But then Green was told by Mr Price, the attorney for Umoya, that the parties to the Umoya/White/Torode/Trust transaction had decided to restructure the transaction by transferring the shares out of Umoya and paying for them *before* the loan was made to the Trust by the Bank. For whatever reason, thus, they decided not to follow the special resolution route proposed by Green. On 16 September 2009 Green wrote to Olivier, to tell him of the restructuring. This is the text of the letter:

> We have had discussions with Mr Gavin Price concerning the agreement he is preparing. He told us that the shares and loan account in [Umoya] had already been acquired and paid for. Accordingly, the loan being raised from the Bank will not

be used to acquire shares but will be used to make a further loan to [Umoya]. That would not contravene Section 38.
Regarding payment of the instalments, we have suggested to the attorney that provision be made for [Umoya] to repay portion of the loan account in monthly instalments equal to the amounts payable to the Bank. The borrower would instruct [Umoya] to make payment directly to the Bank. This again should overcome any difficulties with Section 38. Mr Price will send us a copy of his draft agreement so that we can agree on the format before it is signed. This may necessitate your making an amendment to the Offer Letter. We will also make appropriate adjustments to the Loan Agreement once we have had sight of the agreement.
Jeremy Torode was going to come to Durban tomorrow with documents but we have suggested to him and his attorney agreed that his trip to Durban should be deferred until all the legal issues had been resolved and documents were available for signature.
Perhaps clause 8A(d) of the Offer Letter should be amended to provide that [Umoya] will pay instalments in reduction of the loan account and that the instalments will be paid directly to the Bank on the borrower's behalf in order to service the loan.
Furthermore clause 1 of the Offer Letter should be amended to provide that the loan will be utilized to make a further loan to the company and omit any reference to the acquisition of shareholding.

16 I have quoted so extensively from Green's letter because the insights in Green's letter are important. They show that Green appreciated and communicated to Olivier that in order to eliminate the s 38 problem,

action was required on two levels: firstly, the *nature* of the transaction had to be changed and, secondly, the *documentation* had to be changed to reflect the new nature of the transaction. Green's insights were shared within the Bank by at least four officers including Olivier within the Bank, to whom Green's letter or an in house communication within the Bank conveying the gist of Green's letter, or both, were sent.

17 It is perhaps useful to summarise at this stage what Olivier and all the other persons involved in the transaction knew at this stage. They knew that Umoya was desperately short of money. It could not even service its existing short term debt obligations to its supplier without a capital injection. They knew that if Umoya were to take advantage of the perceived opportunity provided by its business, capital had to be provided urgently. They knew that the existing shareholders either could not or were not prepared to provide this capital. They knew that no financial institution was prepared further to fund Umoya. The only way this could be done was through the Trust, which because of the Gauteng property had access to finance. They knew that the Trust could only be induced to procure the finance and make it available to Umoya if White transferred 45% of the equity in Umoya to Torode.

18 And yet, no more than one day after Olivier had told Torode and White of the s 38 problem and the Bank's refusal to proceed with the transaction in the form that had been agreed between the participants, Umoya told the Bank that the shares *had in fact been* transferred and paid for. To put it at its lowest, this assertion of fact required verification and could not be acted upon without evidence that what Price had told Green had some basis in truth. This was implied in Green's letter to the Bank dated 16 September 2009.

19 The reason Price's assertion required verification was that the very foundation of the transaction as originally contemplated was that Umoya, White and the others who up to then had invested in Umoya were unable or unwilling further to fund Umoya's activities unless a further injection through Torode was forthcoming. Why did this suddenly change after a legal difficulty arose? And most importantly of all, where was the money going to come from to fund the share transfer if it did not come from Torode through the Trust with money borrowed from the Bank?

20 I am simply not prepared to accept, in favour of Olivier, that he did not appreciate that this was so. Any responsible bank officer in Olivier's position would have realised that it was. And Olivier, moreover, did not act without advice. He had the services of Cox Yeats at his disposal.

In his letter, Green, backed up by Price, made plain that the transaction should be deferred and that Torode should not even travel to Durban until, in effect, answers to the questions I have posed emerged. The following passage from Green's letter dated 16 September 2009 bears repeating:

> Jeremy Torode was going to come to Durban tomorrow with documents but we have suggested to him and his attorney agreed that his trip to Durban should be deferred until all the legal issues had been resolved and documents were available for signature.

21 On the same day that he wrote the unpleasant news email, ie 15 September 2009, Olivier wrote to Torode to say that he had managed to negotiate bridging finance of R800 000 to fund the transaction. This was yet another indication that those involved in the transaction were pressed for money and, more particularly, that Torode had no available source of finance for the transaction other than that to be loaned by the Bank.

22 On 16 September 2009, Ms Dustigar, the Bank's internal legal counsel, wrote to a Bank official, Ms Msomi, copying to her the letter from Green of the same date from which I have quoted above and instructing her to "pend the loan agreement because of the proposed

amendments." In a further email to Msomi later the same day, she instructed Msomi to ensure that

> ... the Offer letter is amended to remove all reference to funding for the purpose of purchasing shares in the Guarantor [ie Umoya] - as this will fall foul to S38(1) and thereafter require us to obtain a special resolution as set out in S38(2A) of the Act.

23 On 18 September 2009, Olivier submitted a revised motivation for the loan to the Bank's management for approval. Consistent with the advice of both Green and Dustigar, the revised motivation omitted any reference to the link between the loan and the transfer of the shares in Umoya. The loan, in its revised form, was approved.

24 On 22 September 2009, Green sent Price an email to say:

> The Bank still requires sight of the shareholders agreement. There is no point in Mr Torode coming down until all documents are ready.

25 Price then prepared a sale of shares agreement, which he sent to Olivier in draft under cover of an email of the same date, ie 22 September 2009. The draft sale of shares agreement provided for the sale of 45% of the issued shares in Umoya to the Trust. It was subject

to a suspensive condition regarding the execution of a shareholders' agreement by Umoya, the then shareholders in Umoya and the Trust.

26 The draft sale of shares agreement then proclaimed that as between the parties to the sale of shares agreement (when executed), certain events which had never taken place were to be regarded between these parties in fact (or, more accurately, counterfactually) as having taken place. Firstly, although the document acknowledged that in truth at the time the document was to be executed the shareholders in Umoya were White and Lambert, the sale of shares to the Trust was to be backdated to the "effective date" as defined, ie 1 March 2009.

27 Secondly, four amounts of R250 000 each, which were expressed in the draft to have been paid by the Trust to CES, the creditor pressing Umoya, over the period 14 February to 7 March 2009, would be regarded by them, retrospectively, as the purchase price paid by the Trust for the acquisition of the shares. This meant that the purchase price for the shares would no longer be R2 million as originally agreed between White and Torode but R1 million.

28 In fact, according to Torode, payments totalling the amount of R1 million had been paid at the instance of Torode to CES for the purchase by Torode or the Trust or a company controlled by Torode

called Crystal Wave Properties 3 (Pty) Ltd of terminals over the period 3 to 16 March 2009. The draft committed the parties to the draft to achieve this retrospective adaptation of historical fact by causing the

> necessary entries to be made in the books and records of [Umoya] to give effect to the intention of the parties pursuant to the provisions of this Agreement.

29 The draft sale of shares agreement obliged White, on the date upon which the draft was actually signed by the last of the parties, to deliver to the auditors of Umoya share transfer forms completed by him in negotiable form and other documents, all of which, where appropriate, the Trust was then obliged to sign, thus completing the formalities attendant upon the transfer of the sale shares to the Trust.

30 Price also prepared a draft shareholders' agreement to regulate the new relationship between Umoya, White, Lambert and the Trust. The effective date of the draft shareholders' agreement also proclaimed, counterfactually, that on its signature, its effective date would be 1 March 2009.

31 The sale of shares agreement was drawn subject to the suspensive condition, which under clause 2 could not be waived, that the shareholders' agreement be executed simultaneously or within 48

hours of the signature of the sale of shares agreement by the last party to sign it.

32 The shareholders' agreement, if it had been concluded as drafted, would have reflected White and the Trust as holders of 45% each of the equity in Umoya and Lambert as the holder of the remaining 10%. The draft committed Umoya to procuring a loan to the maximum of R2 million from a bank with the Trust as the actual borrower and to standing surety for the obligations of the Trust to the lender. It also committed Umoya (between the parties to the shareholders' agreement) to be primarily responsible for the repayment of the loan.

33 In fact, the draft sale of shares and shareholders' agreements were never signed. But for reasons not explained in the evidence, Olivier wrote in an email to Green, with copies to other bank officers, on 22 September 2009:

> The said [ie sale of shares] agreement effectively means that the initial amounts paid in Feb & March were for the purchase of the shares, and it stands to reason that the current R 2.0 million is a loan to the shareholder, thus not contravening the relevant section of the Act.

34 By letter dated 23 September 2009, Price wrote to Green regarding the execution of the documents required to achieve the advance of the R2 million by the Bank to the Trust. The letter made no reference to the execution of the draft sale of shares and shareholders' agreements. In a letter of the same date to Olivier, Price again copied to Olivier the "draft" sale of shares and shareholders' agreement.

35 Olivier prepared an amended offer letter (the revised facility). Clause 1 was amended to read: "The facility is for an amount of R2 ... million ... which will be utilised to lend to Umoya ... ." Clause 8A(d) was excised. He also prepared a formal loan agreement, which forms the Bank's cause of action in the present case and was ultimately signed on behalf of the Trust on 25 September 2009 and on behalf of the Bank on 7 October 2009. The revised facility was also signed by both the Bank and by Torode, on behalf of the Trust on 24 or 25 September 2009. The R2 million was paid over to the order of the Trust. I cannot find in the record the precise date on which the R2 million was paid but on the probabilities it was after the formal loan agreement was signed by the bank, ie 7 October 2009, and before a meeting took place at Price's office on 12 October 2009 in relation to Umoya's affairs.

36 The meeting was attended by White, Torode, Lambert, Price, Rosana (*sic*) Hunter (Umoya's financial manager) and Boshoff (a representative of CES). An agenda was prepared for the meeting. The first item on the agenda was the shareholders' agreement. Because of the interlock between the sale of shares and shareholders' agreements, it seems likely that both documents were to be dealt with. Torode was elected to chair the meeting. But it appears from the minutes, which Price drafted, that the business proper of the meeting began with a discussion of item 10, the status of CES and then progressed to a discussion of matters concerning Eskom, possibly agenda item 15.

37 At some stage during the meeting, although there is no reference to it in the minutes, an argument broke out between White and Lambert. The cause of the argument was, according to Torode, whether Lambert's mother would receive some part of the R2 million injected pursuant to the loan from the Bank. White refused to agree to this. The argument became violent. A chair was apparently thrown by one of the disputing parties at the other. The meeting, which had lasted according to the minutes five minutes short of three hours was then adjourned without date.

38 But Umoya did not prosper and some four months later it ceased trading. In the interim, the money advanced to the Trust had been used to pay Umoya's creditors. During this period, Torode was treated for discussion purposes as a shareholder of Umoya. But in fact no shares in Umoya were ever transferred to him, even informally. No written sale agreement or shareholders' agreement was ever concluded. No oral sale agreement or real ("*saaklike*") agreement pursuant to which the 45% shareholding could have been transferred (ceded to) Torode or the Trust was suggested in the evidence. White remained throughout the period relevant to this case the holder of 90% of the issued shares in Umoya.

39 I think, because of certain arguments advanced by counsel for the defendants, I should say something about the pleadings. In its declaration, the Bank pleaded as its cause of action the formal loan agreement, to which the revised offer letter formed an annexure, the mortgage bond under which the Trust put up the property as security and the guarantee executed by Torode.

40 The defendants' plea asserted that the "form and substance" of the initial offer letter formed the basis of the agreement concluded between the parties and that the later variations were never

authorised by the Trust.[2] The plea proceeded to allege that the later amendments, which resulted in the revised offer letter and the formal loan agreement, were effected to disguise their true purpose, which was to simulate the transaction identified in the later agreements and conceal their true purpose: to provide financial assistance to the Trust to acquire 45% of the issued shares in Umoya in contravention of s 38. By reason of the simulation and the contravention of s 38, the formal loan agreement is, so runs paragraph 2 of the plea, unlawful, void and unenforceable.

41 The Bank replicated. The replication alleged knowledge of all concerned prior to the execution of the formal loan agreement that the initial offer letter "may" constitute a contravention of s 38. The replication then proceeds in paragraph 3 to plead that the draft sale agreement was prepared by Price. Paragraph 5 of the replication then asserts that if the facts

> constituting the sale of the shares by .. [the Trust] pleaded in paragraph 3 above are proved in the course of the trial, then the loan agreement cannot amount to a contravention of [s 38].

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2 Ultimately, the defence that the latter agreements were not authorised by the Trust was abandoned.

42 On these pleadings, counsel for the defendants submitted that the Bank had admitted the conclusion of the agreement envisaged in the terms of the draft sale agreement. I may mention that the only witnesses to give evidence in relation to the execution of the draft sale agreement, Price and Torode himself, both said it was not ever executed. And it is clear from my analysis of the pleadings that the Bank did not admit that the draft sale agreement was executed or formed the basis of an agreement between its purported parties. For one thing, the defendants never pleaded that it did, so no admission could have been made. The true import of the replication, in my view, is the assertion that *if* the draft became proved to have progressed from being merely a draft to an agreement between its recited parties, then the agreement so concluded would not give rise to a contravention of s 38.

43 Counsel for the defendants further submitted that in fact the provisions of the initial offer letter prevailed throughout, despite the terms of the revised offer letter and the formal loan agreement and that the true purpose of the guarantee by Umoya was to provide financial assistance as I have set out.[3]

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3 Strictly speaking, I think, the defendants pegged their s 38 defence to the proposition that the operative agreement between the parties remained the initial facility. But it was not suggested in argument that the defence was so limited. I shall therefore proceed on the basis that the defence was intended to apply regardless of the terms of the operative agreement or agreements.

44 I cannot agree with this submission. All the parties, including the Bank, accepted that the form of the transaction as originally conceived fell foul of s 38. They were advised, at least in effect but probably expressly, that if the shares were transferred away from White to Torode *before* the loan agreement was concluded, they could escape the strictures of s 38. They wanted to escape these strictures. The Bank's documentation was amended to cater for the anticipated new form of the transaction.

45 Price testified that he held the view that Torode was entitled to the transfer of the shares by virtue of the stage reached in the negotiations between Torode and White. I do not agree and Torode does not appear ever to have demanded their transfer. But the decisive point at this level is that the terms of the formal loan agreement seen in the context of the revised offer and other surrounding circumstances left it in no doubt that the guarantee provided by Umoya under the loan agreement was not linked to any sale of shares.

46 From this two things relevant to the present enquiry follow. Firstly, the parties to the transaction as it was initially formulated had all agreed not to proceed with the transaction as so initially formulated.

Secondly, at the date of execution of the formal loan agreement, there was no obligation on White to transfer the shares to Torode.

47 The import and reach of s 38, and its predecessor, s 86*bis* of the Companies Act, 46 of 1926, have been authoritatively explained by our courts. The object of the measure is the protection of the creditors of a company. Its purpose is to avoid the company's fund of paid-up capital being used 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.[4] The purpose to be determined is the purpose of the company performing the act complained of.[5] Although the prohibition is couched in wide and general terms, there has been a tendency to adopt a much narrower approach to the section.[6] The prohibition comprises two main elements: the giving of financial assistance and the purpose for or connection with which it is given.[7]

48 Only the *direct object* and not the *ultimate goal* of the transaction is relevant. If the direct object is not the provision of financial assistance by the company for the purchase of its shares, then it is irrelevant that

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4 *Lewis v Oneanate (Pty) Ltd* 1992 4 SA 811 A 818A-C

5 *Lipschitz NO v UDC Bank Ltd* 1979 1 SA 789 A 805

6 *Lipschitz NO v UDC Bank Ltd* 1979 1 SA 789 A 797H-798A

7 *Lipschitz NO v UDC Bank Ltd* 1979 1 SA 789 A 799

the ultimate goal was to enable a person to purchase those shares.[8] If the purpose of the provision of the financial assistance was not, or would not be, the giving of financial assistance, then the giving of assistance is not "in connection with" the purchase of the company's shares unless the actual purpose sufficiently resembles the prohibited purpose.[9]

49 Counsel for the defendants correctly accepted that the defendants bore the onus of proving that the transaction was hit by the section.[10] Torode advanced the money to Umoya in the belief that ultimately White would agree to transfer the shares to him. But for whatever reason, after White and Torode agreed no longer to proceed with the transactions evidenced in the initial offer letter or the draft sale of shares agreement or the shareholders' agreement, no agreement was reached between White and Torode for the purchase by Torode of shares in Umoya from White. In fact, the proceeds of the loan from the Bank were used to pay Umoya's creditors and were never used or to be used (there being no agreement in that regard) to procure the transfer of shares in Umoya to Torode.

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8 *Gardner and another v Margo* [2006] 3 All SA 229 SCA para 47

9 *Lipschitz NO v UDC Bank Ltd* 1979 1 SA 789 A 804-5

10 *Evrard v Ross* 1977 2 SA 311 D 317

50 To that extent, the present case is similar to the situation in *Johnson v Johnson and Others*.[11] At p332, the court held that on the facts of that case, neither of the main protagonists could have contravened s 38 *if in fact no purchase of shares took place*. Their intention or belief, the court held, was irrelevant. If such intention or belief had no basis in fact, then any such intention or belief could not alter such facts.

51 In these circumstances, was there a contravention of s 38? The question is more precisely: did Umoya give the guarantee to the Bank for the purpose of or in connection with the purchase by Torode or the Trust of its shares? Factually, the answer is that it did not. Although the initial arrangement was that it would do so, that arrangement was superceded by no more than a loose promise to restructure the transaction so that the transfer of shares would be unlinked from the provision by Torode or the Trust of loan capital. That promise was refined into the draft sale of shares and shareholders' agreements. But for whatever reason, those draft agreements were never signed and the anticipated relationships never materialised. The Trust provided the loan capital to Umoya against nothing more than, at best, an implied undertaking by Umoya to repay it one day. So while even if the *ultimate goal* of the transaction was to provide in the future for

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11 1983 2 SA 324 W

a sale of shares to the Trust,[12] its *direct object* was to generate capital for Umoya. It then follows that the formal loan agreement was not a simulation but expressed the true intention of the parties to that agreement.

52 This conclusion renders it unnecessary to determine the intention or belief of the Bank, White (acting personally and representing Umoya and Torode (representing the Trust). But in case I am wrong in my conclusion that their states of mind are irrelevant, I shall shortly state my views in this regard. I think that all concerned did not particularly care whether the Bank advanced money and took Umoya's guarantee for the purpose of or in connection with the purchase by Torode or the Trust of Umoya's shares. They decided that the transaction as originally formulated ought not to go ahead because they accepted that the transaction as so originally formulated fell foul of s 38. No doubt they hoped that as reformulated, the loan would not contravene the section. But on the part of the Bank, its officials failed to take the elementary step of establishing that the juristic acts envisaged in the draft sale of shares and shareholders' agreements were ever performed. In particular, they were indifferent as to whether the transfer of shares in respect of which the Bank had been advised should not be linked to the loan and the guarantee by Umoya were

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12 A question which we need not decide.

transferred to the Trust before the execution of the formal loan agreement. By their indifference towards the question whether the transaction had been reformulated in fact to escape the reach of s 38, they showed that they were indifferent to whether or not the transaction in fact contravened the section. What they were really concerned about was whether the documents as redrawn *gave the impression* that s 38 was not implicated and whether the Bank's securities in the form of the two guarantees and the mortgage bond were in place.

53 I think that the main purpose of Umoya and White in giving the guarantee was to raise funds to keep Umoya afloat. If this had involved transferring shares to the Trust, I think they would have acquiesced. The Trust, through Torode, was content to allow the proceeds of the loan to be used to keep Umoya afloat and to proceed in the hope that his negotiations with White would come to fruition and the shares would be transferred to him.

54 It follows that the appeal must succeed. The parties agreed that if the Bank was successful in its claim, the amount owed was R2 517 554,57 together with interest accruing on this amount at the Bank's variable prime interest rate (8,5% as at 19 April 2013 plus 55 calculated daily and compounded monthly in arrear from 1 April 2013

to date of payment, both days inclusive. Both the formal loan agreement provided for the Bank to recover costs as between attorney and client.

55 The cross-appeal against the decision by the trial court to non-suit the Trust in its counterclaim was predicated on a finding that the loan agreement was invalid. Having found that the loan agreement was not shown to be invalid, I need not say any more in this regard.

56 It follows therefore that the appeal must succeed and the cross-appeal must fail. I make the following order:

1 The appeal succeeds with costs against the defendants jointly and severally.

2 The cross-appeal is dismissed with costs against the defendants jointly and severally.

3 The order of the court below is altered to read:

3.1 There will be judgment for the plaintiff against the defendants, jointly and severally for R2 517 554,57 together with interest accruing on this amount at the plaintiff's variable prime interest rate (8,5% as at 19 April 2013) plus 5% calculated daily and compounded monthly in arrear from 1 April 2013 to date of payment, both days inclusive.

3.2 Portion 278 (a portion of portion 228) of the Farm Horningklip No.178, registration division IQ, Province of Gauteng in extent 2,0236 hectares, held under deed of transfer no. T116885/06 is declared specially executable.

3.3 The claims in reconvention are dismissed

3.4 The defendants, jointly and severally, must pay the plaintiff's costs of suit on the scale as between attorney and client in relation to the claims both in convention and in reconvention.

NB Tuchten
Judge of the High Court
18 May 2016

I agree.

RG Tolmay
Judge of the High Court
May 2016

I agree.

TAN Makhubele
Acting judge of the High Court
May 2016

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