

REPORTABLE

IN THE KWAZULU-NATAL HIGH COURT, DURBAN
REPUBLIC OF SOUTH AFRICA

CASE NO. 14397/2009

In the matter between:

PROFLOUR (PTY) LIMITED
FIRST APPLICANT
DURBAN GRITS (PTY) LIMITED
SECOND APPLICANT

and

GRINDROD TRADING (PTY) LIMITED
t/a ATLAS TRADING & SHIPPING
FIRST RESPONDENT
NEDBANK LIMITED
SECOND RESPONDENT

JUDGMENT Delivered on 15 December 2009

SWAIN J

[1] What is in issue in this application are the competing rights of the first respondent and the second respondent, in respect of a cession by the first and second applicants of book debts, respectively to each of the respondents.

[2] The cessions in favour of the second respondent by the applicants (the Nedbank cessions) were effected on 22 September

2006 and 11 May 2007 respectively. The sessions in favour of the first respondent by the applicant (the Atlas sessions) were effected on 12 December 2008.

[3] Thereafter, and on 29 May 2009, the applicants each concluded Invoice Discounting Agreements (hereafter referred to as IDA's) with the second respondent.

[4] It is the conclusion of the IDA's which has given rise to the present dispute. The first respondent argues that the effect of the IDA's was to novate and extinguish the Nedbank sessions. A consequence of this is that the Atlas sessions are now the primary sessions in respect of the trade debts, and the first respondent contends that it is accordingly entitled to collect the trade debts of the applicants. The applicants dispute this contention, denying that there was any novation of the Nedbank sessions by the IDA's and seeking declaratory relief and in the alternative, interdictory relief, from this Court, in confirmation of the applicants' contentions. At the hearing I was advised by Mr. Salmon, S.C., who appeared for the applicants, that only declaratory relief was now sought.

[5] The issue therefore requiring resolution at the outset, is whether a novation of the Nedbank sessions was effected by the IDA's.

[6] A primary dispute between the applicants and first respondent in this regard is whether evidence of the subjective intention of the representative of the applicants on this issue, when he signed the IDA's on behalf of the applicants, may be tendered.

[7] The sole director of the applicants, one David Strang, in the applicants' replying affidavit, stated that when he signed the IDA's he had no intention that the agreements should in any way replace the Nedbank cessions, and was unaware of the Atlas cessions. In addition, Natalie Backman on behalf of the second respondent, stated that the second respondent was unaware of the Atlas cessions when a letter (Annexure NB3) was written by the second respondent to the applicants, and when the IDA's were concluded. The statements by Strang elicited an application to strike them out by the first respondent on the basis that this evidence was inadmissible. As regards the statement by Backman and the contents of Annexure NB3, it was submitted that they were likewise inadmissible. The argument advanced by Mr. Harpur, S.C., who together with Mr. Courtsoudis, appeared on behalf of the first respondent, was that it was a rule of interpretation of contracts that direct evidence of a parties' own intention may not be lead.

[8] It is clear that in an action on a contract, the rule of interpretation is to ascertain

"...not what the parties' intention was, but what the language used in the contract means, i.e. what their intention was as expressed in the contract".

Worman v Hughes & Others
1948 (3) SA 495 (A) at 505

"The intention of the parties must be gathered from their language, not from what either of them may have had in mind"

Van Pletzen v Henning
1913 AD 82 at 89

[9] In the case of

Coopers & Lybrand v Bryant
1995 (3) SA 761 (A) at 767 E – 768 E

it was made clear that extrinsic evidence, regarding the surrounding circumstances in which a contract was concluded, may only be led when the language of the contract is ambiguous on the face of it. Direct evidence of the parties' own intention may not however be led.

[10] It is clear that in determining whether a novation has occurred, intention to novate is never presumed

van Coppenhagen v van Coppenhagen
1947 (1) SA 576 (T) at 578 – 581

and that

"The result of the authorities is that the question is one of intention and that, in the absence of any express declaration of the parties, the intention to effect a novation cannot be held to exist except by way of necessary inference from all the circumstances of the case"

Electric Process Engraving & Stereo Co. v Irwin
1940 AD 220 at 226 – 227

The "circumstances of the case" include the conduct of the parties.

French v Sterling Finance Corporation (Pty) Ltd.
1961(4) SA 732 (A) at 736 H

[11] Holmes J A in French's case *supra*, in examining the circumstances of that case, considered the evidence of a witness at a particular meeting, referring to what the witness said in the following terms

"He also said there was no intention of releasing the appellant as guarantor"

specifically in regard to whether a novation had been established.

[12] Consequently, it appears on the basis of this dictum that in order to establish whether a novation has occurred, the Court is entitled to have regard to the conduct of the parties, including any

evidence as to their intention. This enquiry is not limited in the same way as the limitation imposed upon the interpretation of the terms of a contract. I comprehend that the reason for this is that whether one agreement has been novated by another, cannot be found solely within the parameters of the agreements themselves, where the enquiry is whether the terms of the new agreement, are inconsistent with the continued existence of the original right. This is because the essence of the enquiry is to determine the intention, which accompanies the conclusion of the new arrangement.

"It is more likely that a creditor who has an existing enforceable right, will intend, when he enters into any new arrangement in regard thereto, to reinforce rather than destroy that right and accept something else in its place."

(emphasis mine)

Trust Bank of Africa Ltd. v Dhooma
1970(3) SA 304 (N) at 307 D – G

It is therefore necessary that the circumstances of the case be examined, including the conduct of the parties and evidence of their subjective intention. This would be admissible evidence in this context.

[13] The application to strike out these portions of Strang's evidence accordingly fails, as does the objections to the admission of the evidence of Backman and the contents of Annexure NB3.

[14] The weight to be attached to Strang's *ipse dixit* that at the time he signed the IDA's, he had no intention that the agreement should in any way replace the Nedbank cessions (which is denied by the first respondent) has to be examined in the context of all of the evidence. In support of his assertion, he states that neither he (on behalf of the applicants) nor the second respondent, were aware when the IDA's were signed, of the existence of the Atlas cessions. Backman, on behalf of the second respondent, confirms this.

[15] An absence of knowledge of the Atlas cessions, on the part of the applicants and the second respondent, is borne out by the terms of the IDA's. In Clause 16.1.3 the applicants' warrant that the debts sold and ceded in terms of the IDA's, have not been ceded to any other person. Clause 16.3 provides that in the event of the applicants breaching this warranty, the applicants are obliged to procure the cancellation of the right giving rise to the breach, whether by payment of the debt, or otherwise. Consequently, a lack of knowledge of the Atlas cessions, on the part of the applicants and the second respondent, is not a factor supporting an absence of an intention to novate, precisely because the parties made express provision in the IDA's for such an eventuality and the manner of its resolution.

[16] Of greater significance however, is the contents of Annexure NB3 to the affidavit of Backman. This is a letter dated 05 May 2009

written by representatives of the second respondent to the applicants. The letter in essence sets out the basis upon which the second respondent is prepared to conclude the IDA's with the applicants. The terms and conditions contained in this letter were accepted by the applicants.

[17] Of significance in this regard are the provisions of Clause 12 (g) which provide as follows:

"Confirmation from your bankers, Nedbank Business Banking, KZN Region, that session of book debt held for Durban Grits (Pty) Ltd. and Profitour (Pty) Ltd will be cancelled. (This will be resolved internally within the business units)."

[18] This clause makes it clear that no funds will be advanced in terms of the IDA's, until the Nedbank sessions have been cancelled. This clause clearly conveys a common intention that the conclusion of the IDA's will have no effect upon the legal existence of the Nedbank sessions. It is the common intention of the parties that the Nedbank sessions will have to be cancelled, before the second respondent will be obliged to perform in terms of the IDA's, by advancing funds to the applicants.

[19] Admissible evidence, in the form set out above, is not the only criteria in determining whether an intention to novate can be inferred. As pointed out above, whether the terms of the new

arrangement are inconsistent with the continued existence of the original right, also has to be considered.

Trust Bank of Africa Ltd. v Dhooma
1970 (3) SA 304 (N) at 307 F - G

[20] There is a great deal of debate before me in the heads of argument, filed on behalf of the applicants and the first respondent, as to whether the terms of the IDA's are inconsistent with the terms of the Nedbank cessions.

[21] In my view, a detailed analysis is not required because the very nature of the IDA's is inconsistent with the Nedbank cessions. In this regard I agree with the submission of Mr. Harpur, S.C. that the holding of the rights by the second respondent, as security, in terms of the Nedbank cessions, is replaced by a purchase and cession of the same rights, with the right to acquire ownership of these rights on delivery, in terms of the IDA's. It is of the essence of a pledge that the pledged asset is owned by a person other than the creditor.

[22] It seems to me however, that the inconsistency between the terms of the Nedbank cessions and the IDA's, and particularly the inconsistency between the rights held by the second respondent in terms of the Nedbank cessions and the IDA's, was clearly appreciated by the applicants and the second respondent, before

the IDA's were concluded. The agreement between the applicants and the second respondent, as contained in the letter, Annexure NRB3, made direct provision for the resolution of this conflict by providing that the second respondent would not be obliged to perform its obligations and advance money to the applicants, until the Nedbank cessions had been cancelled.

[23] The onus to establish a novation of the Nedbank cessions by the IDA's, lies upon the first respondent who alleges the novation.

Barclays National Bank Ltd. v Smith
1975 (4) SA 675 (N) at 683 B

Clear and cogent proof of novation is required because it involves a waiver of rights

Marendaz v Marendaz
1953 (4) SA 218 (C) at 226 - 227

and where an intention to novate is sought to be established by implication, the intention must be "clear and unequivocal."

Dhooma's case supra at 307 D – G

[24] Regard being had to the foregoing and particularly the expressed intention of Strang on behalf of the applicants, that he never intended a novation, supported as this evidence is by the

contents of the letter Annexure NB3, which specifically provides for a cancellation of the Nedbank cessions, I am satisfied that the first respondent has failed to discharge the onus of establishing the novation relied upon.

[25] The next issue which has to be resolved is whether the second applicant's Nedbank cession in favour of the second respondent is valid. The challenge raised by the first respondent is that the manuscript addition to this cession, reading as follows:

"All present and future debtors only to the value of O D facility at that time"

results in the invalidity of the cession on two grounds:

[25.1] It constitutes an invalid partial cession of debts without the consent of the debtors.

[25.2] The object of the cession is not determinable, as it is not possible to determine which debts are subject to the cession and which are not.

[26] As regards the first ground, Mr. Harpur, S.C. relies upon the decision in

Kotsopoulos v Bilardi

1970 (2) SA (391 (C) at 396 F – G

It is clear that a partial cession of a debt only applies when the debt of a single debtor is split between two creditors by cession. That is not the case here. The book debts of numerous debtors are ceded. As pointed out by the second respondent, all that may conceivably happen is "that one particular debt of the bundle of book debts may be partially ceded". This possibility is obviously insufficient to render the cession invalid.

[27] In my view, the clause means no more and no less, than that a limitation is placed upon the value of the book debt ceded, which at no stage should exceed the current overdraft. This clause is consequently not directed at the identity of the debtors, whose debts are ceded, but at the value of the debts ceded. The identity of the debtors are established in terms of Clause 2 of the cession.

[28] Everything points to such a construction

"the words, the purpose of the transaction and the dictates of business efficacy"

Langston Clothing (Properties) cc v Danco Clothing (Pty) Ltd.
1998 (4) SA 885 (SCA) at 889 F

[29] In my view, the cession effected by the second applicant in favour of the second respondent is valid.

[30] Turning to the next issue namely, whether the Nedbank cessions in favour of the second respondent are out-and-out cessions, and whether the Atlas cessions in favour of the first respondent, are consequently invalid.

[31] It is clear that the effect of a cession in *securitatem debiti* is that

"the principal debt is 'pledged' to the cessionary while the cedent retains what has variously been described as the 'bare *dominium*' or a 'reversionary interest' in the claim against the principal debtor."

Grobler v Oosthuizen

2009 (5) SA 500 (SCA) at paras 15 and 17

The theory that "a cession in *securitatem debiti* is in effect an outright or out-and-out cession on which an undertaking or *pactum fiduciae* is super-imposed that the cessionary will re-cede the principal debt to the cedent on satisfaction of the secured debt" has not been accepted.

Grobler's case *supra* para 17.

[32] The argument of Mr. Salmon, S.C., as I understand it, is that the Nedbank cessions must be construed as out and out cessions, with the result that the Atlas cessions are of no force and effect, because they purport to effect a cession to the first respondent of the very rights ceded by the applicants to the second respondent.

[33] The argument of Mr. Salmon, S.C. that the Nedbank cessions are out and out cessions is based upon the fact that they include a clause to the effect that they survive the temporary extinction of any indebtedness of the cedent to the cessionary. I agree with the submission of Mr. Harpur, S.C. in this regard, that because the Nedbank cessions provide security for both existing and future indebtedness, until cancelled, the clause simply provides for continuation of the security on the temporary extinction of the indebtedness, in order to provide security for future indebtedness.

[34] In addition, as pointed out by Mr. Harpur, S.C., no provision is made in the Nedbank cessions for a re-cession of the debts once the applicants have discharged the secured debt. This is clearly inconsistent with the Nedbank cessions being out-and-out cessions.

[35] As pointed out in Grobler's case *supra* at para 24, absent a clear expression of intention of an alternative form of cession in *securitatem debiti*, the pledge construction must prevail.

[36] I find no such clear expression of intention in the Nedbank cessions, which I accordingly find to be cessions in *securitatem debiti* and not out-and-out cessions. The Atlas cessions in favour of the first respondent are accordingly not invalid on this ground. What was ceded to the first respondent, in terms of the Atlas cessions,

was the reversionary interest held by the applicants in their trade debts.

[37] The next issue to be determined is whether the first respondent is able to exercise the reversionary interest of the applicants in their trade debts, ceded to the first respondent, in terms of the Atlas cessions, by collecting the trade debts of the applicants, before the indebtedness of the applicants to the second respondent has been extinguished.

[38] Mr. Harpur, S.C. submits that the first respondent is entitled to claim performance by the trade debtors of the applicants, once the secured debt has been extinguished, and/or in circumstances where the cessionary chooses not to rely upon the security, or where there is excess after the discharge of the secured debt.

[39] The fact that the second respondent, in the exercise of its "sole and unfettered" discretion in terms of Clause 12 of the Nedbank cessions, may not have relied upon its security, in my view, does not entitle the first respondent to collect the trade debts of the applicants in the interim. In support of his contention in this regard, Mr. Harpur, S.C. referred to the following passage in

"In the case of a pledge, the pledgor can cede his reversionary right (dominion) outright to a second cessionary, in which case the second cessionary becomes the holder of the right on the discharge of the cedent's debt to the first cessionary. The effect of this cession is that if the pledgee (first cessionary) does not make use of the security, the second cessionary automatically becomes entitled to the claim or to the balance of the proceeds after the first cessionary's claim has been satisfied"

[40] I understand the learned author's reference to the first cessionary not making use of the security, simply to mean that the claim of the first cessionary is satisfied by the cedent, without the need for the first cessionary to utilise the security. If a portion of the security is utilised to pay the first cessionary, the second cessionary is entitled "to the balance of the proceeds" of the security. It is therefore quite clear from this passage that the first respondent would only be able to collect the trade debts of the applicant, if the second respondent does not make use of the security, in the event that the second respondent's claim has been settled. When it is borne in mind that all that the first respondent acquired was the applicants' reversionary interest in the applicants' trade debts, which were ceded to the second respondent, the first respondent could only expect to collect the trade debts of the applicants, once the applicants' indebtedness to the second respondent had been extinguished. The second respondent cannot be held to have compromised its security, merely by the exercise of the "sole and unfettered" discretion it possesses, as to the manner in which it asserts its right to the security.

[41] Consequently, the only basis upon which the first respondent would be entitled to set about claiming payment of the trade debts of the applicants, would be if payment by the applicants of their indebtedness to the second respondent, was made.

[42] In the result, the applicants are not entitled to an order declaring that the Atlas cessions are invalid, but are entitled to relief in the alternative form, declaring that the first respondent is not entitled to collect the book debts of the applicants, from the applicants' debtors. At the hearing I was informed that the first respondent does not persist in its contention that the second respondent is a "trade debtor" of the applicant, which entitles the first respondent to collect payment from the second respondent.

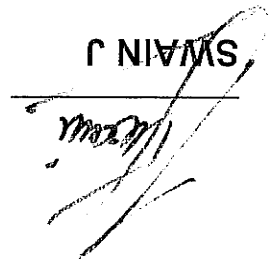
[43] As regards the issue of costs, Mr. Pammenter, S.C., who appeared for the second respondent, advised me that the second respondent did not wish its costs to be paid by any of the other parties.

The order I make is the following:

1. It is declared that pending payment by the applicants of their indebtedness to the second respondent, the first respondent is not entitled, in terms of Annexure D to the founding affidavit

of David Fraser Strang, to collect the book debts of the applicants from the applicants' debtors.

2. The first respondent is ordered to pay the costs of the applicants.


SWAIN J

Appearances: /

Appearances:

For the Applicants	:	Mr. R. Salmon, S.C.
Instructed by	:	De Villiers Evans & Pett Durban
For the 1st Respondent	:	Mr. G. Harpur, S.C.
Instructed by	:	Garlick & Bousfield Inc. Durban
For the 2nd Respondent	:	Mr. C. J. Pammenter, S.C.
Instructed by	:	Shepstone & Wylie Durban
Date of Hearing	:	13 November 2009
Date of Filing of Judgment :		15 December 2009