

RISK AND OPPORTUNITIES CONNECTED TO THE CREDIT LEGISLATION ON MOVABLE PROPERTY: A CASE STUDY

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Abstract

The purpose of this paper is to determine to what extent should a lease of movable property fall within the ambit of the National Credit Act. The paper analyses the courts' decisions regarding leases of movable properties, and further adds value to the existing scholarship. Courts are not ready to entertain extrinsic evidence in the cases where it contradicts the terms of an agreement. Parties should make sure that their contractual provisions are clear and unambiguous. Such provisions depict the notion that a lease of a movable property should fall within the ambit of the National Credit Act, hereinafter called NCA. And in such circumstances that qualifies it in terms of the Act ought to be met. In terms of section 8(4) of the NCA, a lease of movable property should by no means exclude the provision that ownership will pass to the lessee upon payment of the final rental instalment. Alternatively upon meeting certain conditions as determined by parties. One should therefore be able to differentiate leases in terms of the NCA and leases as defined by common law. Thus, one cannot try to qualify common law leases within the context of section 8(4) of the NCA where the original intention was an ordinary common law lease agreement. The Court in the case of *ABSA Technology v Michael's Bid House* concluded that the NCA was not applicable to leases of movable property in certain circumstances. It is the findings of this paper that courts, recognize lease of movable property.

Keywords: Incidental Credit Agreement, Rental Agreement, National Credit Act (NCA), Lease of Movable Property

1. INTRODUCTION

The principal issue before the Appeal Court was whether the rental agreement between the parties was a lease. A lease as defined in the National Credit Act is the very anti-thesis of a lease. Thus, the Appeal Court indicated that rental agreements generally are leases. The issue to be further determined, *inter alia*, is whether extrinsic evidence can be invited to prove the original intentions of parties, in particular where parties have not complied with provisions of section 8(4). The provisions of section 8(4) determine which contracts constitute credit agreements including leases. It should be with regards to a movable lease contract that they might have intended that such leases should fall within the ambit of the National Credit Act. Should it be regarded as an incidental agreement simply because another party believed it was so without it having to comply with the pre-requisites of an incidental agreement in terms of the National Credit Act. Thus, the paper purposed to analyse the *Michael Bid House case* in order to illustrate the way in which the Court addressed issues related to the lease of movable property.

The decision of *Absa Technology v Michael's Bid House*³ was an appeal from the South Gauteng High Court in South Africa. The Appeal Court had to

decide whether a lease of movable property was governed by the provisions of section 8(4) of the National Credit Act (hereinafter referred to as the NCA)⁴ under certain circumstances. The High Court held that the agreement was a lease since the representative of the lessee believed that ownership of the machine hired would somehow pass to the lessee on termination of the lease agreement. And that the provisions of the NCA regulating notice to the defaulting lessee were operative. The Supreme Court overturned the High Court's decision asserting that the provisions of a movable property lease agreement intended to be covered by the NCA, should comply with provisions of section 8(4). Further that such lease agreement should be apparent (*ex facie*) from the face of the contract itself.

2. RESEARCH METHODOLOGY

This research has adopted doctrinal legal research approach as a data collection method. This method is also known as the "black letter law". Pearce, Cambell and Harding (1999) define doctrinal legal research approach as a research which provides a systematic exposition of the rules governing a particular legal category, analysis of the relationship between rules and explains areas of difficult and

³ (212/2012) [2013] ZASCA 10 (26 February 2013)

⁴ National Credit Act 34 of 2005

perhaps predicts future developments. Therefore, doctrinal method basically means reading, interpreting and analysing of legal resource in details.

3. THE FACTS OF THE MICHAEL BID HOUSE CASE

The first respondent is Michael`s Bid House CC. The second respondent is Michael Rose, an estate agent who conducted a business through the first respondent. He intended to acquire a colour printing machine for the Close Corporation and also to print pamphlets for the other estate agents in the area of Randfontein, Gauteng, South Africa. The second respondent consulted with Mr Vosloo of Westrand Office Equipment who suggested two ways of financing the machine since the Close Corporation could not afford to purchase the machine. Rose elected the option of paying a monthly instalment of R2 878 to 'finance this machine with full maintenance and service and toner supplied for the full 36 month contract'. Furthermore Vosloo indicated in the written quotation that Westrand could arrange 'finance' through Sapor Rentals (Pty) Ltd. On 3 July 2008 both Sapor and Rose on behalf of the Close Corporation signed a 'master rental agreement in terms of which Rose was to pay the aforesaid amount of R2 878 per month for the period of three years. Rose also signed suretyship on behalf of the Close Corporation, hereinafter referred to as CC. The contract commenced on 3 July 2008 and the aforesaid machine was delivered to the CC and installed. On 8 July Sapor ceded its rights under the rental agreement to Absa technology Finance Solutions (Pty) Ltd and the copy was delivered to Rose on 28 July 2008. On 9 July 2008 the CC paid the first instalment to Sapor. On 28 July 2008 Rose indicated to Sapor that he was not satisfied with the printer and the failure to supply toner, that he had been misled into entering into rental agreement and that he was cancelling it. Rose paid the second and last instalment on 8 August 2008.

In November 2008 Absa Technology instituted an action at South Gauteng High Court of South Africa for payment of arrear and future rentals against the CC and Rose as surety in the amount of R111 533. Rose and the CC raised a number of defences in their plea. However, they did not plead rectification or that the rental agreement was simulated or that the contract had been induced by fraud. They only pleaded that Sapor was in breach of the agreement because Westrand failed to deliver toner for the machine, surprisingly not showing that Sapor was a Westrand agent in that regard. However, Westrand was liquidated.

3.1. The High Court'S Ruling

The Court per Beasley J held that prior discussion between Rose and Westrand were inadmissible in the face of written agreement. There was a clause in the rental agreement for the parole evidence rule. It should also be noted that the CC acknowledged that it was referred to Sapor by Westrand which bought the machine. The Court found that the agreement in issue was not a true sale, despite its written provisions to the contrary. And that it was a real agreement between the parties, further that it was a credit agreement for the purpose of the NCA. The

Court further indicated that as such Absa Technology as a lessor had to give notice and proceed under section 129 and 130 of the NCA to the CC as lessee and Rose as a surety before enforcing the agreement. The High Court did not give judgment on merits. It held that Absa Technology should not set the matter down until complied with section 129 and 130. The High Court granted a leave to appeal against this decision.

3.2. The Supreme Court of Appeal's Ruling

The Appeal Court invoked the decision of *Health Professions Council of South Africa v Emergency Medical Supplies and Trading CC t/a EMS*⁵ in which it was stated that the Court will not entertain an appeal against part of an order even if it has disposed of a point of law. Accordingly the lease will not be disposed of until Absa Technology has complied with section 129 and 130 of the NCA because there might be further appeal on other aspects. Interestingly the counsel for Absa Technology convinced the Court that there was nothing further that the High Court could adjudicate on. And, further that if the appeal was heard, and turn to be successful it would be the end of the matter. However, if it is dismissed then Absa Technology would comply with section 129 and 130. Thereafter, the judgment would be granted against CC and Rose.

The Appeal Court was of the view that the judgment of the High Court affected many financial institutions and a class of contracts in respect of which the applicability of the NCA warrants clarification. The Court also held that in any event the time would be wasted if it declined to hear the appeal before compliance with section 129 and 130. Should it be decided on the appeal after judgment, that such compliance was unnecessary, it would therefore confirm that indeed time has been wasted. It is on this basis that the Appeal Court was willing to proceed to entertain the matter.

Section 8(4) determines which contracts constitute credit agreements including leases. The principal issue before the Appeal Court was whether the rental agreement between the parties was a lease. Thus the Appeal Court indicated that rental agreement generally are leases but a lease as defined in the NCA is the very anti-thesis of a lease. The Court went on to examine the meaning of lease in section 1 of the NCA:

"Lease" means an agreement in terms of which-

- (a) temporary possession of any movable property is delivered to or at the direction of the consumer, or the right to use any such property is granted to or at the direction of the consumer;
- (b) payment for the possession or use of that property is-
 - (i) Made on an agreed or determined periodic basis during the life of the agreement or
 - (ii) Deferred in whole or in part for any period during the life of the agreement;
 - (c) interest, fees or other charges are payable to the credit provider in respect of the agreement, or the amount that has been deferred; and
 - (d) at the end of the term of the agreement, ownership of that property either-

⁵ 2010 (6) SA 469 (SCA)

- (i) passes to the consumer absolutely; or
- (ii) passes to the consumer upon satisfaction of the specific conditions set out in the agreement’.

The court was of the view that a true lease in which the lessee should return the property on the termination of the agreement and the relationship between the lessor and lessee is not governed by the definition of the credit agreement in the NCA.

Accordingly the Appeal Court had to adjudicate on the following three issues:

- (a) Whether the rental agreement was governed by section 8(4)(e) of the NCA;
- (b) Whether the rental agreement was governed by section 8(4)(f);
- (c) Whether the rental agreement was an incidental credit agreement in terms of the NCA.

With regard to the first issue the High Court found that the agreement between the parties was lease in terms of the NCA. It relied on the evidence of Rose and Absa Technology’s witnesses as to whether the ownership would pass to the CC on the termination of the agreement. The High Court confined itself to the question as to whether or not the rental agreement was a lease. In this regard the High Court admitted the evidence despite Absa technology objecting to that evidence to be led.

The Appeal Court went on to examine the relevant terms of the contract, which read as follows:

‘Hirer [first Sapor and then by virtue of the cession Absa Technology] shall at all times be and remain the owner of the goods and neither User [the CC] nor any other person on his behalf shall at any stage before or after the expiry of this agreement or after termination thereof acquire ownership of the goods’

‘Notwithstanding the provisions of this agreement should User in breach of its obligations fail to return the goods on termination of this agreement then in addition to any other claims that Hirer may have against User pursuant thereto, User shall be liable to continue to pay rentals to Hirer as if the agreement had not been so terminated’

‘User shall, on termination of this agreement, return the goods together with all applicable documents to Hirer at user’s cost and expense’.

The Appeal Court indicated that the requirement that ownership of the goods must pass at the end of the lease was not met as expressly stated in the definition of the lease in the NCA. The Appeal Court also questioned the basis upon which the High Court admitted extrinsic evidence that contradicted the terms of the agreement. The learned judge accepted an approach that if evidence was available to the true intention of the parties which is not reflected in the agreement then it was acceptable to vary its terms to bring it within the ambit of the NCA. According to the Appeal Court the High Court examined the decisions of *Absa technology Finance Solutions Ltd v Pabi’s Guest CC*⁶ and *Absa Technology Finance Solutions v Viljoen t/a Wonderhoek Enterprises*⁷ wherein the court appeared to have considered ‘extrinsic evidence as to what the lessees had intended in order to determine the nature of the transaction in issue’. In *Pabi* the court held that in the absence of evidence as to the content of the contract, the court could not go

beyond the terms of the contract and that section 8(4)(f) applied in accordance with the content of the contract and not by virtue of its name. It should be noted that the court in *Pabi* also held that it ‘must have regard to the substance of the contract, not merely its form’. The High Court referred to the decision of *Ticker v Ginsberg*⁸ also *Bridgeway v Markham* wherein the court determined whether a contract fell within the provisions of section 8(4). In *Bridgeway* the court was of the view that when the court determine the nature of the contract, it ‘must scrutinize the whole course of the parties dealings’.

The Appeal Court indicated that the reliance in *Padi’s* and *Bridgeway* on *Tucker* is misplaced. The court said it would not admit evidence as to what the parties intended to mean if that had the effect of altering the terms in which the parties agreed upon.

The Appeal Court said the correct approach to the admissibility of the parol evidence is the one stated by Harms DP in *KPMG Chartered Accountants SA v Securefin Ltd.*⁹ The court in *Securefin* asserted the following: Firstly, if a document was intended to provide a complete memorial of a jural act, extrinsic evidence may not contradict, add to or modify its meaning (*Johnson v Leal*).¹⁰ Secondly, interpretation is a matter of law and not of fact and accordingly interpretation is a matter for the court and not for witnesses (Hodge M Malek (ed) *Phipson on evidence*).¹¹ Thirdly, rules of admissibility of evidence do not depend on the nature of document, whether statute, contract or patent (*Johnson & Johnson (Pty) Ltd v Kimberly-Clark Corporation and Kimberly-Clark of South Africa (Pty) Ltd*).¹² Fourthly, the extent in which evidence may be admissible to contextualise the document or for the purpose of identification ‘one must use it as conservatively as possible, *Delmas Milling Co Ltd v Du Plessis*.¹³

The Appeal Court held that the High Court erred in allowing evidence as to the parties’ understanding of the rental agreement particularly to the passing of ownership of the machine by *Absa Technology and Rose*. According to the Appeal Court, such evidence should have been ruled as being inadmissible. The Appeal Court on this issue concluded that the written agreement signed by both parties is a lease as it is understood in common law and not a lease for the purpose of section 8(4) of the NCA.

The court went on to adjudicate on the second issue as to whether rental agreement was governed by the provisions of section 8(4)(f) of the NCA. Section 8(4)(f) provides that an agreement irrespective of its form constitutes a credit transaction if it is any other agreement, other than a credit facility or credit guarantee, in terms of which payment of an amount owed by one person to another is deferred, and any charge, fee or interest is payable to the credit provider in respect of the agreement or the amount that has been deferred. In the High Court, Rose and CC argued that the credit agreement falls within the ambit of section 8(4)(f). The High Court rejected the argument by both Rose

⁶ 2011 (6) SA 606 (FB)
⁷ 2012 (3) SA 149 (GNP)

⁸ 1962 (2) SA 58 (W) at 62F-H

⁹ 2009 (4) SA 399 (SCA)

¹⁰ 1980 (3) SA 927 (A) at 943B

¹¹ (Hodge M Malek (ed) *Phipson on evidence* (16 ed 2005) paras 33-64).

¹² 1985 BP 126 (A) [1985] ZASCA 132

¹³ 1955 (3) SA 447 (A) at 455B-C

and CC and accepted the approach that was followed in *Absa Technology Finance Solutions v Viljoen t/a Wonderhoek Enterprises*.¹⁴ The court in *Viljoen* indicated that in this type of rental agreement there was no question of deferral of the obligation to pay monthly rental because payment was not postponed. The Appeal Court agreed with the High Court when it referred to the decision of *Viljoen* that if the legislature indeed intended to bring such lease within the NCA as a credit transaction it could have easily done so by using plain and unambiguous language. The Appeal Court concluded that the rental agreement was not a credit agreement in terms of section 8(4)(f).

The Appeal Court went on to decide on the third issue, namely as to whether rental agreement was an incidental credit agreement in terms of the NCA. It was contended by Rose and CC that the agreement was an incidental credit agreement in terms of the NCA irrespective of its form over a period where either a fee, charge or interest become payable when the account has not been paid or where two prices are quoted for settlement of the account, the lower price being payable if the account is paid by a determined date and the higher price being payable if the price is not paid by that date. On this aspect the Appeal Court agreed with High Court. It held that rental agreement did not meet the test in the former case because no account or service was rendered. According to the Appeal Court rental had to be paid in terms of the agreement and no account was necessary. Thus, the court concluded that it would be strange to exclude common law leases from its ambit and bring them within the context of section 8(4)(f). The Appeal Court also stated that Absa technology was not required to comply with the provisions of section 129 and 130 of the NCA. It was therefore ordered that Rose and the CC were to pay an amount of R111 533.98.

CONCLUSION

The decision of *Absa Technology v Michael's Bid House* sets a precedent in the legal research pertaining to rental of movable properties. The court correctly entertained this appeal as it does affect many financial institutions and that the applicability of the NCA in this regards warrants much clarification. It is therefore important that one considers the reasoning by the Appeal Court. The Appeal Court clearly indicated that the High Court should not have allowed and relied on the evidence of Rose and Absa Technology witnesses to the effect that ownership of the machine would pass to the CC on termination of the agreement. That was the parties' understanding of the rental agreement and not exactly as in the terms of the contract. The High Court then erred in allowing such evidence despite Absa Technology objecting to that evidence to be led. Secondly, the pre-requisite in section 8(4) that ownership of the goods must pass in terms of the agreement to the lessee at the end of the lease was not met. The Appeal Court held that the approach followed in *Pabi's* and *Bridgeway* was not correct. In this regard the Appeal Court invoked the correct approach used by this court with regard to the admissibility of parole evidence. The Appeal Court

concluded that the written agreement signed by both parties was a lease as it is understood in common law and not a lease for the purpose of section 8(4) of the NCA. On the second issue as to whether the rental agreement was governed by the provisions of section 8(4)(f) of the NCA, the Appeal Court correctly agreed with the High Court, referring to the decision of *Viljoen*, that if the legislature intended to bring such lease within the NCA as a credit transaction, it could easily have done so by using plain and unambiguous language. With regard to the third issue as to whether rental agreement was incidental credit agreement in terms of the NCA the Appeal Court concluded that it would be strange to exclude common law leases from its ambit and bring them with the context of section 8(4)(f). This paper clarifies the legal position relating to common law leases and rental agreements governed by the provisions of section 8(4)(f). It plays an important role for practitioners to take note of discrepancies relating to leases of movable properties.

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¹⁴ 2012 (3) SA 149 (GNP)