FUNDING INITIATIVES INTERNATIONAL (PRIVATE) LIMITED
versus
CONSTANTINE MABAUDI

HIGH COURT OF ZIMBABWE
PATEL J
HARARE, 1 to 2 March 2006 and 19 April 2007

Civil Trial

Mrs *Nyemba*, for the plaintiff
Mr *Ncube*, for the defendant

PATEL J: The plaintiff in this matter claims payment in the sum of $120 million as the balance due in respect of money advanced to the defendant in April 2003. The defendant disputes this claim and counterclaims an amount of $24 million as having been overpaid to the plaintiff under their loan arrangement.

Evidence for the Plaintiff

Stephen Hove, the Managing Director of the plaintiff, testified that the plaintiff was a registered money-lending company [as evidenced by Exhibit 7]. By letter dated the 25th of March 2003 [Exhibit 1] the defendant applied for a loan of $25 million for 14 days. The loan agreement was concluded between the parties on the 7th of April 2003 once the defendant had signed the plaintiff's offer letters [Exhibits 2A & 2B].

On the due date of the 21st of April 2003 the defendant was unable to pay the principal sum and agreed interest. The parties then agreed over the telephone to extend the repayment period for a further 14 days at a higher rate of interest. The defendant confirmed the extension by letter dated the 8th of May 2003 [Exhibit 3]. At the same time he tendered by way of security the title deeds in respect of

his property in Ruwa, an acknowledgement of debt and other related documents [Exhibits 4A, 4B, 4C, 4D & 4E].

The defendant was again unable to pay by the due date and sought more time to repay the loan as per his letter of the 1st of August 2003 [Exhibit 5]. Consequently, a further acknowledgement of debt was executed in respect of the same transaction on the 1st of August 2003 [Exhibit 6]. The first loan including interest was capitalised and advanced again as a fresh loan with the date of repayment being agreed as the 1st of September 2003.

The defendant did not repay on the due date but instead forwarded a cheque for $61,645,994.00 on the 9th of December 2003. As at that date, the defendant's account had an outstanding balance of $117,348,490.00 which was reduced by the cheque payment to $55,702,496.00. As at the 31st of January 2004, the balance due had risen to $120,546,585.00 and this was the amount claimed in the summons.

Under cross-examination, Hove accepted that paragraph C of Exhibit 6 stipulated an interest rate of 30% per annum and a service fee of 13.5% per month. On the defendant's statement of account [Exhibit 8] these charges were not differentiated but lumped together for easier accounting purposes. As from the 8th of December 2003 the interest rate as reflected on Exhibit 8 was altered to 650% per annum. Subsequently, the rate was reduced to 450% per annum with effect from the 1st of January 2004. According to Hove, these changes were effected in accordance with the parties' agreement and because the prior restriction on money-lenders interest rates had been removed. In this respect he referred to paragraphs 3 and 9(g) of Exhibit 2B which allowed for the variation of interest rates in terms of prevailing legislation. However, he conceded that Exhibit 6 did not contain any reference to a variable interest rate as charged on the money market.

Evidence for the Defendant

The defendant, Constantine Mabaudi, is a banker by profession. He accepted that he had borrowed the sum of $25 million from the plaintiff on the 7th of April 2003 on the terms set out in Exhibits 2A and 2B and that he had defaulted twice in repaying that loan.

Subsequently, on the 1st of August 2003, he signed the second acknowledgement of debt for $61 million [Exhibit 6]. This was not a new loan or an additional advance of money but a statement of his indebtedness in respect of the original loan of $25 million. The sum of $61 million comprised the capital and interest plus service fees and other charges on the original loan. He accepted that he had agreed to the interest rates and other charges stipulated in Exhibit 6. After signing Exhibit 6 he also signed a blank post-dated cheque [Exhibit 12] at the plaintiff's insistence.

On the 9th of December 2003 he paid the sum of $61,645,994.00 by way of cheque. This figure was a departure from the amount due in terms of Exhibit 8. The cheque was accompanied by a letter of the same date [Exhibit 10] which stated that the payment was in full and final settlement of all the amounts due under the loan. The plaintiff accepted the cheque but wrote a letter on the 11th of December 2003 [Exhibit 9] demanding a further $55 million.

According to Mabaudi, although Exhibit 2B provided for the variation of interest rates in accordance with legislation, the prescribed rate of 30% for money-lenders has not changed. Money-lenders were not part of the larger money market comprising banks and other financial institutions. They were required to lend their own money and were not permitted to borrow from others in order to on-lend.

The defendant's counterclaim was for the sum of $24 million that he had overpaid to the plaintiff. This figure was calculated by applying to the loan a rate of 35% per annum for interest and administrative charges as per prevailing legislation [Exhibit 11]. The defendant also

sought the return of his title deeds that were surrendered to the plaintiff as security for the loan.

The Issues

The issues for determination in this matter are as follows:-

1. Whether or not the acknowledgement of debt signed by the parties on the 1st of August 2003 novated the defendant's debt.
2. Whether the acknowledgement of debt is valid and enforceable.
3. Whether or not the plaintiff was entitled to charge interest as agreed or in terms of the law.
4. Whether or not the defendant is indebted to the plaintiff in the sum of $120,546, 585.84.
5. Whether or not the defendant overpaid the plaintiff by the sum of $24,681,621.27 or by any other amount.

Effect of Acknowledgement of Debt

By virtue of paragraph B of the acknowledgement of debt [Exhibit 6], the defendant acknowledged his liability to the plaintiff as at the 1st of August 2003 and his indebtedness in the sum of $61,586,666.56 as being the capital amount due to the plaintiff. Pursuant to paragraph C, the defendant undertook to pay the capital amount together with interest at 30% per annum as well as service fees at the rate of 13.5% per month, calculated monthly in arrears from the 1st of August 2003 to the date of payment in full. In terms of clauses 4 and 6 of Exhibit 6, the defendant renounced the benefit of all legal exceptions and accepted that the acknowledgement constituted the entire agreement between the parties.

As I read them, the terms of Exhibit 6 make it quite clear that its purpose and effect was to capitalise the original loan of $25 million

[Exhibits 2A & 2B] and the interest accrued thereon. At the same time, the defendant acknowledged his indebtedness in the new agreed amount of $61 million. In essence, Exhibit 6 constituted a novation of the defendant's original debt by way of a *novatio voluntaria* whereby interest began to run afresh up to the double in accordance with the *in duplum* rule. In the words of GILLESPIE J in *Commercial Bank of Zimbabwe Ltd v MM Builders & Suppliers (Pvt) Ltd & Anor* 1996 (2) ZLR 420 (H) at 466:

> "This is not necessarily to say that the parties are unable, *ex post facto*, that is once the debt is called up, to agree a novation of the debt. ..... This new debt would then be repayable on agreed terms. This would be a true capitalisation of the interest on the previous debt. ..... [A] novation after the event permits the debtor the informed choice of increasing his possible indebtedness or of taking advantage of the cessation of accrual of interest."

Validity of Acknowledgement of Debt

The defendant *in casu* challenges the validity of Exhibit 6 on a number of grounds. As a rule, where an out-of-court compromise or settlement is agreed between the parties, it is generally not permissible to go behind the transaction in order to test the validity of the original loan or credit facility – unless the compromise agreement itself expressly or impliedly contains a reservation of rights under the original agreement. See *Dennis Peters Investments v Ollerenshaw & Ors* 1977 (1) SA 197 (W) at 202-203; *Nagar v Nagar* 1982 (2) SA 263 (ZH) at 267. See also *Georgias & Anor v Standard Chartered Finance Zimbabwe Ltd* 1998 (2) ZLR 488 (S) at 498, where GUBBAY CJ stated as follows:

> "Compromise, or *transactio*, is the settlement by agreement of disputed obligations, or of a lawsuit the issue of which is uncertain. The parties agree to regulate their intention in a particular way, each receding from his previous position and conceding something — either diminishing his claim or increasing his liability. ..... The purpose of compromise is to

> end doubt and to avoid the inconvenience and risk inherent in resorting to the methods of resolving disputes. Its effect is the same as *res judicata* on a judgment given by consent. It extinguishes *ipso jure* any cause of action that previously may have existed between the parties, unless the right to rely thereon was reserved. ..... As it brings legal proceedings already instituted to an end, a party sued on a compromise is not entitled to raise defences to the original cause of action. ..... But a compromise induced by fraud, duress, *justus* error, misrepresentation, or some other ground for rescission, is voidable at the instance of the aggrieved party, even if made an order of court. ..... Unlike novation, a compromise is binding on the parties even though the original contract was invalid or even illegal."

The learned Chief Justice further observed, at 198, that:

> "In my view, the case of *Dennis Peters Investments (Pty) Ltd v Ollerenshaw & Ors* 1977 (1) SA 197 (W) is analogous and the reasoning apposite. The facts were that the plaintiff company sued the three defendants jointly and severally for provisional sentence. The action was based on a written acknowledgement of debt in terms whereof the defendants admitted owing the plaintiff the sum of R6 500 for moneys lent and advanced. They averred that the payments to them were in fact substantially money-lending transactions upon which the plaintiff had charged usurious rates of interest. The acknowledgment of debt, however, had been given to the plaintiff pursuant to a settlement of its claims. .....
>
> It is important to note that even assuming the defendants had been charged usurious rates of interest contrary to law and offensive to good morals and public policy, the learned judge was not prepared to go behind the acknowledgement of debt."

Two of the authorities referred to in the *Georgias* case are directly pertinent to the facts of the present case insofar as concerns the distinction between a compromise and a novation. In *Syfrets Mortgage Nominees Ltd v Cape St Francis Hotels (Pty) Ltd* 1991 (3) SA 276 (SEC) at 288E-F, the point was made that the agreement under review:

> "was clearly a compromise as distinct from a novation where one admittedly valid contract is replaced by another valid contract".

The distinction is articulated more succinctly in *Hamilton v van Zyl* 1983 (4) SA 379 (ECD) at 383D-E:

> "In pointing out the difference between novation and compromise (*transactio*) Wessels on *The Law of Contract in South Africa* 2nd ed. vol. II para. 2458 states:
>
> > 'There is a great similarity between *transactio* and novation and as a rule the principles which apply to the latter apply to the former. (*Voet* 46.2.3). There is however this difference between the two. When parties novate they intend to replace a valid contract by another valid contract, and if therefore the novated contract is invalid, the novating contract is, as a general rule, of no effect. If, however, a claim is made upon a contract, about the validity of which the defendant has a doubt, and a *transactio* follows, the defendant cannot upset the compromise on the ground that the agreement which was compromised was in fact invalid.'."

In the instant case, it is common cause that the acknowledgement of debt [Exhibit 6] did not eventuate from any dispute or doubt as to the defendant's indebtedness; nor was it concluded pursuant to any out-of-court settlement or compromise. As I have already indicated, it clearly constituted a novation of the original loan agreement [Exhibits 2A & 2B]. Accordingly, in keeping with the authorities that I have cited, the validity of the acknowledgement of debt is predicated on the legality of the original loan. It is therefore pertinent and necessary to enquire into and scrutinise the propriety of the original transaction.

Moneylending and Rates of Interest Act [*Chapter 14:14*]

Section 8 of Chapter 14:14 regulates the maximum rates of interest chargeable by moneylenders as follows:

> "(1) No lender shall stipulate for, demand or receive from the borrower interest at a rate greater than the prescribed rate of interest.
>
> (2) Any lender who contravenes subsection (1) shall be guilty of an offence and liable to a fine not exceeding level seven or to imprisonment for a period not exceeding one year or to both such fine and such imprisonment."

Insofar as concerns civil claims, section 9 of the Act precludes the recovery of excess interest. In its relevant portions, it provides:

> "(1) No lender shall, under any contract of loan of money, obtain judgment for or recover from the borrower an amount which exceeds a capital amount which, added to any sum already paid in respect of the capital debt, equals the sum actually advanced to and received by the borrower under the contract plus—
>
> (a) interest at a rate not exceeding the prescribed rate of interest ; and
>
> (b) .....; and
>
> (c) .....; and
>
> (d) .....
>
> (2) No lender shall in any proceedings against a borrower recover, as for loss, damage or expense alleged to have been incurred in connection with any loan of money, any sum not included in an amount recoverable in respect of such loan under subsection (1).
>
> (3) No lender shall in any proceedings in insolvency, assignment or liquidation be allowed to prove, in respect of any loan of money, for any sum for which he could not in terms of this section have obtained judgment."

Where a borrower has paid excess interest, section 11 entitles him to recover such excess in the following terms:

> "Any person who, under or in connection with any contract of loan of money, has paid to the lender an amount which exceeds the amount which could upon such contract have been recovered from such person under any provision of this Act shall be entitled, at any time within two years after the date of the payment, to recover from the person to whom he made it a sum equal to the amount of the excess."

The established principle of our law is that anything done contrary to a direct statutory prohibition is generally void and of no legal effect. The mere prohibition operates to nullify the act, particularly where it is visited with a criminal sanction. See *Schierhout v Minister of Justice* 1926 AD 99, at 109; *Metro Western Cape (Pty) Ltd v Ross* 1986 (3) SA 181 (AD) at 188-189. Whether this principle equally applies to the terms of a settlement or compromise founded on an

illegal agreement is a moot point, having regard to the authorities discussed earlier. It is not necessary for me to decide this point in view of my finding that the acknowledgement of debt *in casu* was not a compromise but a novation of the original loan agreement. For present purposes, therefore, both transactions are susceptible to scrutiny for compliance with the provisions of Chapter 14:14.

Having regard to the direct and unambiguous prohibition spelt out in section 8 of the Act, I am in no doubt that its provisions cannot be waived by agreement and that any contractual stipulation to the contrary must be treated as being null and void *ab initio*. Moreover, as is made crystal clear in section 9, any interest charged or agreed in excess of the prescribed maximum is unenforceable and irrecoverable, whether through civil proceedings or otherwise. Consequently, where usurious interest is charged in contravention of the Act, the borrower is entitled, in terms of section 11, to recover the excess amount paid within a period of two years after the date of payment.

Rates of Interest and Fees Chargeable

Section 4 of the Moneylending and Rates of Interest Regulations 1985, as amended by section 2 of Statutory Instrument 126 of 1993, prescribes the maximum rates of interest chargeable by moneylenders and other lenders governed by the Act. For the purposes of the present loan, being in excess of $100,000.00 at the relevant time, the maximum rate prescribed by section 4(1)(d) is a rate equivalent to either the prevailing re-discount rate or the current rate in respect of bankers' acceptances, whichever is the higher. In addition, the lender may charge "a maximum of three *per centum* for administrative costs".

There does not appear to be any real dispute between the parties as to the applicable rate of interest chargeable on the debt *in casu*. The rate stipulated in both Exhibit 2B (clause 3) and Exhibit 6

(clause C) was 30% *per annum* and no evidence or argument was presented by either party to contest that rate. I will therefore proceed on the basis that the rate of 30% *per annum* was within the prescribed maximum rate of interest chargeable at the relevant time.

The plaintiff in this matter, *qua* registered moneylender, was clearly bound by the provisions of Chapter 14:14 and could not legally charge or recover any amount in excess of the prescribed maximum rates of interest and administrative costs. In this respect, it is abundantly clear that the interest rates of 650% and 450% *per annum*, levied by the plaintiff in December 2003 and January 2004 respectively (as per Exhibit 8), are patently illegal and unenforceable. They are not only clearly prohibited by the law but also not even contemplated in the written agreements between the parties.

The interest rate of 30% *per annum* fixed on the original loan and the acknowledgement of debt is accepted as being within the permissible limit and must therefore be treated as being fully enforceable and recoverable. However, the "front end fees" amounting to $3,750,000.00 referred to in Exhibit 2A and capitalised in Exhibit 2B as well as the "default interest" at 16.5% per month and "service fees" at 6.25% per month fixed in Exhibit 2B fall beyond the prescribed rates and charges. The same applies to the "service fees" at the rate of 13.5% per month stipulated in Exhibit 6. All of these amounts constitute illegal charges and, as such, they cannot be enforced or recovered. The plaintiff must accordingly be confined to claim interest at the rate of 30% *per annum* plus administrative costs of 3% on the capital amount.

Respective Claims of Both Parties

Having regard to all of the above, I calculate the amounts due to the plaintiff to be as follows : the original capital sum of $25,000,000; interest at the rate of 30% *per annum* on the capital sum, calculated

over a period of eight months from the 7th of April 2003 to the 9th of December 2003, amounting to $5,000,000; and administrative costs at the flat rate of 3% on the capital sum amounting to $750,000.

The total amount due to the plaintiff as thus calculated is the sum of $30,750,000. The defendant has already paid the plaintiff an amount of $61,645,994.00. It follows that the plaintiff has been overpaid by the defendant by a sum of $30,895,994.00. The latter is therefore entitled to recover that amount as well as the title deeds to his property which are presently held by the plaintiff as security for the original loan.

In the result, the plaintiff's claim is dismissed and the defendant's claim in reconvention is upheld. Accordingly, judgement is entered in favour of the defendant as against the plaintiff as follows:

The defendant be and is hereby ordered:

(i) to pay to the defendant the sum of $30,895.99 (revalued), together with interest thereon at the prescribed rate calculated from the 9th of December 2003 to the date of payment in full, and costs of suit;

(ii) to surrender to the defendant the title deeds to Stand No. 5579, Zimre Park, Ruwa, within 5 days from the date of this order.

Nyemba & Associates, plaintiff's legal practitioners
Gill, Godlonton & Gerrans, defendant's legal practitioners