A suretyship can be defined as a contract whereby a person, namely the surety, undertakes to the creditor of another person, namely the principal debtor, that as accessory to the principal debtor’s liability, the surety two will be liable for the debt. In this article we will be dealing with two aspects; namely, the principal obligation of a suretyship and incorporation by reference in respect of a suretyship.

RECENT CASE LAW DEVELOPMENTS

A recent judgment was handed down in the Supreme Court of Appeal relating to the validity of a contract of suretyship. In the case of G A Odendal & Another v Structured Mezzanine Investments (482/13) [2014] ZASCA 89, the facts were as follows:

During February 2008, Structured Mezzanine Investments Limited (“SMI”) approved a loan application made by the trustees on behalf of the FXT Property Trust (“the Trust”) in the amount of R10 million to partly fund a sectional title scheme development by the Trust.

One of the conditions attached to the approval of the loan was that the trustees of the Trust had to bind themselves as sureties for all the Trusts obligations owed to SMI. The trustees of the Trust signed the suretyships. The loan agreement was signed by SMI after the suretyships had been signed by the sureties.

THE SURETYSHIP SIGNED BY THE APPELLANTS INCLUDED THE FOLLOWING MATERIAL CLAUSES:

Clause 1: ‘the payment on demand of any sum of money together with all costs and charges including legal costs as between attorney and own client which the Debtor may now or in future owe to SMI arising from the Loan agreement concluded between SMI and the Debtor on or about April 2008...’

Clause 4: ‘This suretyship shall remain in force and effect as a continuing covering suretyship for the present and future indebtedness and obligations of the debtor to SMI, notwithstanding any interim fluctuation in the extinction (for any period) or of indebtedness and subsequent incurring of any new indebtedness or obligation by the Debtor to SMI and notwithstanding the death or other legal disability of any of us until terminated in accordance with the terms hereof.’
Two arguments were raised in the case, which are discussed herein below:

**PRINCIPAL OBLIGATION DOES NOT HAVE TO EXIST WHEN A SURETYSHIP IS CONCLUDED**

What is evident from the aforementioned definition of a contract of suretyship is that a suretyship is an accessory obligation. A valid principal obligation must exist between the creditor and principal debtor. However, the whole issue of a suretyship being an accessory obligation seems to be shrouded in mystery.

Logic dictates that a principal obligation must exist at the time the suretyship is executed, due to the accessory nature of a suretyship. However, the truth of the matter is that a principal obligation need not exist when the suretyship is executed.

The court in the case of GA Odendal v Structured Mezzanine Investments (482/13) 2014 ZA SCA 89 had the opportunity to again confirm the position. The gist of the first argument on behalf of the appellants was that the principal debt was not in existence at the time of the conclusion of the suretyship. The court confirmed that, "It is indeed so that a contract of suretyship is accessory in the sense that it is of the essence of suretyship that there be a valid principal obligation. (that of the debtor to the creditor)."

The court however held that the fact that a loan agreement had not yet been concluded between the debtor and creditor was in itself no barrier to the potential validity of the contract of suretyship. The court referred to the position as was pointed out by Corbett JA in Trust Bank of Africa Ltd v Frysch 1977 (3) SA 562 (A) at 584 G-H that, '… it is not essential that the principal obligation exists at the time when the suretyship contract is entered into. A suretyship may be contracted with reference to the principal obligation which is to come into existence in the future.'

**DOCTRINE OF INCORPORATION BY REFERENCE**

Section 6 of the General Law Amendment Act 50 of 1956 ("the Act") reads as follows:

“No contract of suretyship entered into after the commencement of this Act, shall be valid, unless the terms thereof are embodied in a written document signed by or on behalf of the surety...”

The one requirement that emanates from section 6 of the Act is that the “terms” of the suretyship MUST be embodied in a written document. It has been widely accepted in our law that these terms referred to in section 6 of the Act in essence means the identity of the creditor, that of the principal debtor, that of the surety, as well as the nature and amount of the principal debt.

However can it be said that a suretyship can be saved by the doctrine of incorporation by reference from invalidity if one of the terms is omitted.

The doctrine of incorporation as applicable to suretyships, is to the effect that when the suretyship itself fails to contain an essential term, but the term is contained in another document, the other document may be incorporated in the suretyship agreement. The Supreme Court of Appeal previously held that there was no reason why the doctrine of incorporation by reference could not apply to suretyships.

The gist of the second argument raised by the appellants in the Odendal case was that the agreement referred to in the contract of suretyship, being the one giving rise to the principal debt, is not the one to which reference is made in the suretyship, but that it refers to a loan agreement already concluded. However, it was undisputed that at the time of the signing of the suretyship and despite the reference therein to an already concluded agreement, no such agreement was concluded.

Further to the appellants' contention, SMI correctly stated that irrespective of the deficiency pertaining to the wording of the suretyship, the suretyship is in fact saved by the reference to the loan agreement that was ultimately concluded between the parties and which was incorporated into the deed of suretyship by making reference thereto.

The court in dealing with the validity of the contract of suretyship and in applying the doctrine of incorporation by reference went as far as stating that it is now settled in our law that a deed of suretyship may nonetheless be saved from invalidity by virtue of the doctrine of incorporation by reference, where the essential terms of the contract of suretyship has been omitted.

On the facts of the case, the court found in favour of SMI's contention that the suretyship is valid and complies with Section 6 of the Act as the written loan agreement is incorporated into the suretyship which expressly refers thereto.

**CONCLUSION**

In respect of the first issue raised in the aforesaid case it is safe to state for a suretyship to be valid, a principal obligation need not exist at the time the suretyship is executed, but the surety is not liable until there is a principal debtor and debt. The surety may even withdraw his suretyship prior to the principal debtor and the principal debt coming into existence. The drafter of the suretyship will be wise to insert a clause in the suretyship that the surety cannot withdraw his surety, if the suretyship is signed prior to the existence of the principal obligation or obligations, especially if a continuing covering suretyship is signed by the surety for the current and any future indebtedness of the principal debtor to the creditor.

Further to the aforesaid and in respect of the second aspect discussed it is evident that there can no longer be any misconceptions surrounding section 6 of the Act. The application of the doctrine of incorporation by reference with regard to suretyships, is to the effect that incomplete suretyships may be given a new life by virtue of the doctrine of incorporation by reference.
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